



COUNCIL CHAMBERS

17555 PEAK AVENUE MORGAN HILL CALIFORNIA 95037

COUNCIL MEMBERS	REDEVELOPMENT AGENCY	FINANCING AUTHORITY
Dennis Kennedy, Mayor	Dennis Kennedy, Chair	Dennis Kennedy, President
Greg Sellers, Mayor Pro Tempore	Greg Sellers, Vice-Chair	Greg Sellers, Vice-President
Larry Carr, Council Member	Larry Carr, Agency Member	Larry Carr, Authority Commissioner
Hedy Chang, Council Member	Hedy Chang, Agency Member	Hedy Chang, Authority Commissioner
Steve Tate, Council Member	Steve Tate, Agency Member	Steve Tate, Authority Commissioner

WEDNESDAY, OCTOBER 6, 2004

AGENDA

JOINT MEETING

CITY COUNCIL SPECIAL AND REGULAR MEETING

and

REDEVELOPMENT AGENCY SPECIAL MEETING

and

MORGAN HILL FINANCE AUTHORITY COMMISSION

5:30 P.M.

A Special Meeting of the City Council and Redevelopment Agency, is called at 5:30 P.M. for the Purpose of Conducting Closed Sessions and City business. A Special meeting of the Morgan Hill Financing Authority Commission will be called at 7:00 p.m. to conduct City business.

**Dennis Kennedy, Mayor, Chairman, and
President of the Financing Authority Commission**

City of Morgan Hill
Special and Regular City Council,
Special Redevelopment Agency and
Morgan Hill Financing Authority Commission Meeting
October 6, 2004
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CALL TO ORDER

(Mayor/Chairperson/President Kennedy)

ROLL CALL ATTENDANCE

(City Clerk/Agency Secretary/Authority Secretary Torrez)

DECLARATION OF POSTING OF AGENDA

Per Government Code 54954.2

(City Clerk/Agency Secretary/ Authority Secretary Torrez)

5:30 P.M.

City Council Action and Redevelopment Agency Action

CLOSED SESSION:

1.

CONFERENCE WITH LEGAL COUNSEL - ANTICIPATED LITIGATION

Authority:	Government Code Sections 54956.9(b) & (c)
Number of Potential Cases:	4

2.

PUBLIC EMPLOYEE PERFORMANCE EVALUATION

Legal Authority	Government Code 54957
Public Employee Performance Evaluation:	City Manager
Attendees:	City Council, City Manager

OPPORTUNITY FOR PUBLIC COMMENT

ADJOURN TO CLOSED SESSION

RECONVENE

CLOSED SESSION ANNOUNCEMENT

7:00 P.M.

SILENT INVOCATION

PLEDGE OF ALLEGIANCE

PROCLAMATIONS

Domestic Violence Awareness Month
Community Solutions - Amy Molica

PRESENTATION

Flu Shots
Health Trust - Cynthia York

CITY COUNCIL REPORT

Council Member Carr

CITY COUNCIL SUB-COMMITTEE REPORTS

CITY MANAGER'S REPORT

CITY ATTORNEY'S REPORT

OTHER REPORTS

PUBLIC COMMENT

NOW IS THE TIME FOR COMMENTS FROM THE PUBLIC REGARDING ITEMS NOT ON THIS AGENDA.

(See notice attached to the end of this agenda.)

**PUBLIC COMMENTS ON ITEMS APPEARING ON THIS AGENDA WILL BE TAKEN AT THE TIME
THE ITEM IS ADDRESSED BY THE COUNCIL. PLEASE COMPLETE A SPEAKER CARD AND
PRESENT IT TO THE CITY CLERK.**

(See notice attached to the end of this agenda.)

**PLEASE SUBMIT WRITTEN CORRESPONDENCE TO THE CITY CLERK/AGENCY SECRETARY. THE
CITY CLERK/AGENCY SECRETARY WILL FORWARD CORRESPONDENCE TO THE CITY
COUNCIL/REDEVELOPMENT AGENCY.**

City Council Action

CONSENT CALENDAR:

ITEMS 1-15 The Consent Calendar may be acted upon with one motion, a second and the vote, by each respective Agency. The Consent Calendar items are of a routine or generally uncontested nature and may be acted upon with one motion. Pursuant to Section 5.1 of the City Council Rules of Conduct, any member of the Council or public may request to have an item pulled from the Consent Calendar to be acted upon individually.

Time Estimate

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Consent Calendar: 1 - 10 Minutes

1. **TEMPORARY APPOINTMENT TO SOCCER SUBCOMMITTEE** 1
 Recommended Action(s): Appoint Mayor Dennis Kennedy as a Temporary Replacement for Council Member Hedy Chang on the Soccer Subcommittee.
2. **REPORT OF THE LEGISLATIVE SUBCOMMITTEE** 3
 Recommended Action(s): Support Proposition 1A and Proposition 59 on the November 2, 2004 Statewide Ballot.
3. **EMPLOYMENT AGREEMENT WITH THE CITY ATTORNEY** 5
 Recommended Action(s): Approve the Second Amendment to the Employment Agreement with the City Attorney, Extending the Term of the Agreement to September 1, 2006.

Time Estimate **Page**
Consent Calendar: 1 - 10 Minutes

4. **SECOND AMENDMENT TO AGREEMENT WITH THE STROMBOTNE LAW FIRM**..... 19
Recommended Action(s): Authorize the City Manager to Execute a Second Amendment to Agreement with the Strombotne Law Firm.

5. **SECOND AMENDMENT TO AGREEMENT WITH THE LAW FIRM OF JORGENSEN, SIEGEL, McCLURE & FLEGEL, LLP**..... 31
Recommended Action(s): Authorize the City Manager to Execute a Second Amendment to Agreement with the Law Firm of Jorgenson, Siegel, McClure & Flegel, LLP.

6. **APPROVAL OF REIMBURSEMENT AGREEMENT WITH PRAVIN PATEL FOR 16995 CONDIT ROAD** 43
Recommended Action(s):
 1. **Approve** an Appropriation of \$41,313 from the Current Year Unappropriated Measure C – Capital Improvement Project Fund Balance for Reimbursement of Installation of Curb and Gutter, Sidewalk, Street Pavement, Striping, and Electroliers along the Southeast Frontage of 16995 Condit Road; and
 2. **Authorize** the City Manager to Execute the Reimbursement Agreement on Behalf of the City, Subject to Review and Approval by the City Attorney.

7. **REUSE GRANT AUTHORIZATION**..... 47
Recommended Action(s): Authorize the City Manager to Execute all Necessary Documents; Including, but not Limited to, Applications, Agreements Subject to Review and Approval of City Attorney, Amendments, and Payment Requests to Secure Grant Funds and to Implement and Carry Out the Purposes Specified in the Grant.

8. **APPROVAL OF AMENDMENT TO PROFESSIONAL SERVICES CONTRACT FOR THE BUTTERFIELD BOULEVARD NORTH CONNECTION FEASIBILITY STUDY** 51
Recommended Action(s): Authorize the City Manager to Execute an Amendment in the Amount of \$11,120 to the City’s Professional Services Agreement with Fehr and Peers to Study Alignment and Rail Crossing Alternatives for the Northerly Segment of Butterfield Boulevard.

9. **APPROVAL OF SUBDIVISION IMPROVEMENT AGREEMENT WITH MORGAN HILL DEVELOPMENT PARTNERS, L.P. – SUTTER PLACE, APN: 726-25-012 & 029**..... 57
Recommended Action(s):
 1. **Approve** the Subdivision Improvement Agreement; and
 2. **Authorize** the City Manager to Sign the Agreement on Behalf of the City with Morgan Hill Development Partners, L.P., Digital Drive (APN: 726-25-012 & 029).

10. **RECISSION OF WATER SUPPLY EMERGENCY RESOLUTION AND STATUS OF PERCHLORATE REMOVAL PLANTS**..... 69
Recommended Action(s):
 1. **Adopt** the Resolution Ending the Water Supply Emergency; and
 2. **Accept** the Status Report on Perchlorate Removal Plants.

Time Estimate

Consent Calendar: 1 - 10 Minutes

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11. [**ADOPT ORDINANCE NO. 1695, NEW SERIES**](#)73
Recommended Action(s): Waive the Reading, and Adopt Ordinance No. 1695, New Series, and Declare That Said Title, Which Appears on the Public Agenda, Shall be Determined to Have Been Read by Title and Further Reading Waived; Title as Follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM ML, LIGHT INDUSTRIAL TO PLANNED UNIT DEVELOPMENT FOR A 7.72-ACRE PARCEL LOCATED AT THE NORTHWEST CORNER OF COCHRANE ROAD AND MADRONE PARKWAY IN THE MADRONE BUSINESS PARK (APN 726-33-028)(ZA-04-11: COCHRANE - TBI).**

12. [**ADOPT ORDINANCE NO. 1696, NEW SERIES**](#)79
Recommended Action(s): Waive the Reading, and Adopt Ordinance No. 1696, New Series, and Declare That Said Title, Which Appears on the Public Agenda, Shall be Determined to Have Been Read by Title and Further Reading Waived; Title as Follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM PUD, RESEARCH AND DEVELOPMENT/MANUFACTURING TO PUD, R3 MEDIUM DENSITY RESIDENTIAL FOR TWO PARCELS TOTALING 15.78 ACRES IN SIZE, LOCATED AT THE SOUTHEAST CORNER OF COCHRANE ROAD AND MONTEREY ROAD IN THE MORGAN HILL RANCH BUSINESS PARK (APNs 726-25-076 & -077) (ZA-04-09: BUTTERFIELD – SOUTH VALLEY DEVELOPERS).**

13. [**ADOPT ORDINANCE NO. 1697, NEW SERIES**](#)85
Recommended Action(s): Waive the Reading, and Adopt Ordinance No. 1697, New Series, and Declare That Said Title, Which Appears on the Public Agenda, Shall be Determined to Have Been Read by Title and Further Reading Waived; Title as Follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A SET OF DEVELOPMENT STANDARDS AND ARCHITECTURAL GUIDE LINES FOR THE DE PAUL (FORMERLY SAINT LOUISE) HEALTH CENTER. (APNs 728-031-005, 006, 012 & 013) (ZA-04-02: COCHRANE-ASSISTED LIVING CENTER).**

14. [**ADOPT ORDINANCE NO. 1698, NEW SERIES**](#)101
Recommended Action(s): Waive the Reading, and Adopt Ordinance No. 1698, New Series, and Declare That Said Title, Which Appears on the Public Agenda, Shall be Determined to Have Been Read by Title and Further Reading Waived; Title as Follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A DEVELOPMENT AGREEMENT WITH DAN GAMEL, INC. FOR THE EXPANSION OF DAN GAMEL’S MORGAN HILL RECREATIONAL VEHICLE (RV) CENTER.**

15. [**RE-BUDGETING 2003-2004 PROJECTS/PROGRAMS**](#) 105
Recommended Action(s): Approve the Re-budgeting of 2003-2004 Project/Program Costs in the 2004-2005 Budget.

City Council and Redevelopment Agency Action

CONSENT CALENDAR:

ITEMS 16-17

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	Consent Calendar: 1 - 10 Minutes	
16.	<u>APPROVE JOINT SPECIAL AND REGULAR CITY COUNCIL AND SPECIAL REDEVELOPMENT AGENCY MEETING MINUTES OF SEPTEMBER 15, 2004</u>	125
17.	<u>APPROVE JOINT SPECIAL AND REGULAR REDEVELOPMENT AGENCY AND SPECIAL CITY COUNCIL MEETING MINUTES OF SEPTEMBER 22, 2004</u>	149

City Council Action

PUBLIC HEARINGS:

	Time Estimate	Page
18.	5 Minutes	
	<u>DEVELOPMENT AGREEMENT, DA-04-03: DeWITT-LATALA</u>	161
	Public Hearing Opened. Please Limit Your Remarks to 3 Minutes. Public Hearing Closed Council Discussion. Action- <u>Motion to Waive</u> the Reading in Full of Development Agreement Ordinance. Action- <u>Motion to Introduce</u> Development Agreement Ordinance by Title Only. (Roll Call Vote)	
19.	10 Minutes	
	<u>ZONING AMENDMENT, ZAA-03-13: CITY OF MORGAN HILL – ATTACHED HOUSING ZONING TEXT</u>	185
	Public Hearing Opened. Please Limit Your Remarks to 3 Minutes. Public Hearing Closed Council Discussion. Action- <u>Motion to Waive</u> the Reading in Full of Ordinance. Action- <u>Motion to Introduce</u> Ordinance by Title Only. (Roll Call Vote)	

City Council Action

OTHER BUSINESS:

	Time Estimate	Page
20.	5 Minutes	
	<u>LIVESTOCK REGULATIONS</u>	215
	<u>Recommended Action(s): Request</u> the Planning Commission to Consider Revisions to the Livestock Regulations in Residential and Commercial Zones.	

City Council and Redevelopment Agency Action

OTHER BUSINESS:

	Time Estimate		Page
21.	10 Minutes	<u>LEASE WITH THE CALIFORNIA YOUTH SOCCER ASSOCIATION (CYSA)</u>	219
		<u>Recommended Action(s):</u> <u>Provide</u> Parameters for Negotiating a Lease Extension with CYSA to Continue Using the Future Location of the Sports Complex as a CYSA Regional Soccer Complex.	

City Council and Financing Authority Action

OTHER BUSINESS:

	Time Estimate		Page
22.	5 Minutes	<u>ISSUANCE OF BONDS FOR WATER PROJECTS</u>	221
		<u>Recommended Action(s):</u>	
		<u>Acting as City Council:</u>	
		1. <u>Adopt</u> Resolution Approving as to Form and Authorizing the Execution and Delivery of Certain Documents in Connection with the Sale and Issuance of Morgan Hill Financing Authority Water Revenue Bonds.	
		<u>Acting as Financing Authority:</u>	
		2. <u>Adopt</u> Resolution Authorizing the Issuance, Sale, and Delivery of Water Revenue Bonds and Approving Certain Documents.	
		<u>Acting as City Council:</u>	
		3. <u>Authorize</u> the City Manager, on Behalf of the City, to Enter Into Agreements With RBC Dain Rauscher Inc. for Financial Advisory Services and with Richards, Watson & Gershon for Bond Counsel/Disclosure Counsel Services, Subject to Review and Approval by the City Attorney.	

FUTURE COUNCIL-INITIATED AGENDA ITEMS:

Note: in accordance with Government Code Section 54954.2(a), there shall be no discussion, debate and/or action taken on any request other than providing direction to staff to place the matter of business on a future agenda.

ADJOURNMENT



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

TEMPORARY APPOINTMENT TO SOCCER SUBCOMMITTEE

RECOMMENDED ACTION(S): Appoint Mayor Dennis Kennedy as a temporary replacement for Council Member Hedy Chang on the Soccer Subcommittee.

EXECUTIVE SUMMARY:

Council Member Hedy Chang is currently one of two council members participating on the Soccer Subcommittee that is reviewing aspects of the San Jose/Sobrato regional soccer complex. It is important that this subcommittee continues to meet. Therefore, due to Council Member Chang's current temporary absence, I recommend that I serve in her place until her return or a permanent appointment is made.

FISCAL IMPACT: NONE

Agenda Item #1

**Recommended and
Submitted By:**

Dennis Kennedy, Mayor



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item #2

**Prepared and
Submitted By:**

City Manager

REPORT OF THE LEGISLATIVE SUBCOMMITTEE

RECOMMENDED ACTION(S): Support Propositions 1A and 59 on the November 2, 2004 statewide ballot.

EXECUTIVE SUMMARY:

At Council's direction, the Legislative Subcommittee has reviewed all of the State Propositions that will appear on the November 2 ballot. As in the past, we believe the Council should focus only on those that have direct impact on city government.

We recommend that the Council support Proposition 1A (Protection of Local Revenues) which would amend the Constitution to restrict the State's ability to raid local government funding, including the City's share of existing sales taxes, property taxes, and Motor Vehicle License Fees. Proposition 1A is the result of a bipartisan agreement with the Governor and Legislature to provide permanent constitutional protection in exchange for two (2) more years of shifting local revenue to support the State budget.

The Council's Finance and Audit Committee has reviewed the specific implications for Morgan Hill and our Sustainable Budget Strategy. It is clear the protections of Proposition 1A are essential to accomplishment of our budget goals.

We also recommend that the Council support Proposition 59 (Public Records, Open Meetings) which would amend the Constitution to replace and strengthen several statutes relating to open meetings and the public right to access documents and records. Proposition 59 creates a constitutional right for the public to access government information. Proposition 59 requires a government entity to demonstrate to a somewhat greater extent than current law why information requested by the public should be kept private.

Morgan Hill has always supported open and accessible government and the constitutional protections of Proposition 59 will accomplish that objective.

FISCAL IMPACT: NONE



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item #3

**Recommended and
Submitted By:**

Mayor

EMPLOYMENT AGREEMENT WITH THE CITY ATTORNEY

RECOMMENDED ACTIONS:

Approve the Second Amendment to the Employment Agreement with the City Attorney extending the term of the agreement to September 1, 2006.

EXECUTIVE SUMMARY:

On November 20, 2002, the City entered into an Employment Agreement with Helene L. Leichter employing Ms. Leichter as the City Attorney for the City of Morgan Hill and General Counsel for the Redevelopment Agency. The term of said Employment Agreement expires on September 1, 2005. I recommend that the City Council approve the attached Second Amendment to Employment Agreement extending the term of Ms. Leichter's Employment Agreement one year beyond the current expiration date to September 1, 2006.

FISCAL IMPACT

None.



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

SECOND AMENDMENT TO AGREEMENT WITH THE STROMBOTNE LAW FIRM

RECOMMENDED ACTIONS:

Authorize the City Manager to execute a Second Amendment to Agreement with the Strombotne Law Firm.

EXECUTIVE SUMMARY:

On June 7, 2004, the City contracted with the Strombotne Law Firm to represent the City's interest in a construction dispute with Stevelle Construction Company, Inc., involving the new Morgan Hill Police Facility. The parties are attempting to reach a negotiated settlement. In the interim, two subcontractors have filed suit against the City for enforcement of Stop Notices. The current contract is insufficient to cover the fees and costs associated with continued negotiations of this matter and defending the City against the lawsuits filed by the subcontractors. Staff recommends that Council approve the attached Second Amendment to Agreement increasing the contract amount to \$50,000. This amount should be sufficient to cover current estimated pre-litigation fees and costs.

FISCAL IMPACT:

The cost of this agreement can be accommodated in the City Attorney's Office budget. No additional appropriation is necessary at this time.

Agenda Item # 4

Prepared By:

(Title)

Approved By:

(Department Director)

Submitted By:

City Manager



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

SECOND AMENDMENT TO AGREEMENT WITH THE LAW FIRM OF JORGENSEN, SIEGEL, McCLURE & FLEGEL, LLP

RECOMMENDED ACTIONS:

Authorize the City Manager to execute a Second Amended Agreement with the law firm of Jorgenson, Siegel, McClure & Flegel, LLP.

EXECUTIVE SUMMARY:

On March 30, 2004, the City entered into an agreement with the law firm of Jorgenson, Siegel, McClure & Flegel, LLP, to provide general legal services. Said services include matters relating to the city's Below Market Rate Housing Program, land use issues, tort litigation and from time-to-time perform the duties of the Acting City Attorney. The current contract is insufficient to cover the fees and expenses necessary to continue representation of the City. Therefore, staff is recommending that Council approve the attached Second Amendment to Agreement increasing the contract amount to \$125,000. This amount should be sufficient to cover the anticipated fees and costs.

FISCAL IMPACT:

The cost of this Amendment to Agreement can be accommodated in the City Attorney's Office budget. No additional appropriation is necessary at this time.

Agenda Item # 5

Prepared By:

(Title)

Approved By:

**(Department
Director)**

Submitted By:

City Manager



CITY COUNCIL STAFF REPORT

MEETING DATE: *October 6, 2004*

APPROVAL OF REIMBURSEMENT AGREEMENT WITH PRAVIN PATEL FOR 16995 CONDIT ROAD

RECOMMENDED ACTION:

1. Approve an appropriation of \$41,313 from the current year unappropriated Measure C – Capital Improvement Project fund balance for reimbursement of installation of curb and gutter, sidewalk, street pavement, striping, and electroliers along the southeast frontage of 16995 Condit Road.
2. Authorize the City Manager to execute the Reimbursement Agreement on behalf of the City subject to review and approval by the City Attorney.

EXECUTIVE SUMMARY: Pravin Patel is developing the Miniature Golf facility at 16825 Condit Road (see attached location map). In addition to the standard off-site improvements across his project frontage, the developer was conditioned to install 314 linear feet of curb and gutter, sidewalk, street pavement, striping, and two electroliers along the southeast frontage of 16995 Condit Road. By completing the 314 linear feet of frontage improvements, the west frontage of Condit Road would have continuous curb and gutter, sidewalk, and electroliers from Dunne Avenue to Tennant Avenue.

On occasion, developers are conditioned to construct public improvements in locations where there is a need but no foreseeable development to complete them. The City collects fees as part of the Measure C (formerly Measure P) development process to fund those situations. In this case, Mr. Patel will construct the needed improvements and then be reimbursed by the City.

Pravin Patel is requesting reimbursement from the City for all costs associated with the installation of curb and gutter, sidewalk, street pavement, striping, and two electroliers. The cost for the installation of 314 linear feet of curb and gutter, sidewalk, street pavement, striping, and two electroliers including a 10% contingency is \$41,313.

Staff recommends that Council approve the developer's reimbursement request.

FISCAL IMPACT: The \$41,313 cost to install curb and gutter, sidewalk, street pavement, striping, and electroliers will be funded with unappropriated 346 (Measure C – Capital Improvement Program) funds.

Agenda Item # 6

Prepared By:

Assistant Engineer

Approved By:

Public Works Director

Submitted By:

City Manager



CITY COUNCIL STAFF REPORT

MEETING DATE: *October 6, 2004*

REUSE GRANT AUTHORIZATION

RECOMMENDED ACTION(S): Authorize the City Manager to execute all necessary documents, including but not limited to, applications, agreements subject to review and approval of City Attorney, amendments, and payment requests to secure grant funds and to implement and carry out the purposes specified in the grant.

EXECUTIVE SUMMARY: The City has been assisting local businesses reduce their waste disposal for several years as a foundation of the City's waste diversion efforts. Through the City's contracts with Environmental Planning Consultants, local businesses benefit from hands-on technical expertise and advice in reducing waste generation, reusing byproducts, and identifying recycling markets for their discards. These activities result in opportunities for businesses to reduce their garbage disposal bills, reduce their material input costs, and conserve natural resources. The City, naturally, benefits from their reduced waste disposal.

The California Integrated Waste Management Board has announced the availability of specific grants to support the expansion of "reuse opportunities." Reuse is the step on the waste management hierarchy that describes taking a discarded material and putting it to a new use without physically transforming the material into something new. Staff is preparing a grant application to expand the technical assistance opportunities available to local businesses specifically as they relate to reuse. This assistance will result in a large number of new ongoing exchanges of materials that will divert waste for many years to come. In addition, the assistance will result in local business staff thinking about reuse and identifying additional reuse opportunities on their own in the future.

Staff recommends that the Council approve the attached resolution authorizing the City Manager to execute all necessary documents, including but not limited to, applications, agreements, amendments, and payment requests to secure grant funds and to implement and carry out the purposes specified in the grant.

FISCAL IMPACT: If the grant application is successful, the City will receive \$18,320 in grant funds and will spend a total of \$39,520 on the project. Of the remaining \$21,200, staff will bring back a request for the appropriation of \$18,320 from the fund balance of the Environmental Programs Fund and \$2,880 will be in-kind grant administration activities that will be funded out of the approved budget for Environmental Programs.

Agenda Item # 7

Prepared By:

Program Administrator

Approved By:

Public Works Director

Submitted By:

City Manager

RESOLUTION NO.

**A RESOLUTION OF THE CITY COUNCIL OF THE CITY
OF MORGAN HILL AUTHORIZING THE SUBMITTAL OF
A REUSE ASSISTANCE GRANT**

WHEREAS, Public Resources Code *Section 42000* authorizes the California Integrated Waste Management Board to conduct market development activities to strengthen demand by manufacturers and end-use consumers for recyclable materials collected by municipalities, nonprofit organizations, and private entities; and

WHEREAS, the concept of reuse is an integrated approach, which encompasses integrated waste management objectives such as building materials efficiency, construction and demolition waste reduction, and maximization of reused- and recycled-content building and landscaping materials; and

WHEREAS, on May 18-19, 2004 the California Integrated Waste Management Board approved the Scoring Criteria and Evaluation Process for the Reuse Assistance Grants; and

WHEREAS, the California Integrated Waste Management Board will enter into an agreement with the Grantee for development of the project;

NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Morgan Hill that staff is authorized to submit an application to the California Integrated Waste Management Board for a Reuse Assistance Grant. The City Manager is hereby authorized and empowered to execute all necessary documents, including but not limited to, applications, agreements, amendments, and payment requests to secure grant funds and to implement and carry out the purposes specified in the grant; and

BE IT FURTHER RESOLVED by the City Council of the City of Morgan Hill that the City intends to approve the appropriation of matching funds if the grant is awarded to the City by the California Integrated Waste Management Board

PASSED AND ADOPTED by the City Council of Morgan Hill at a Regular Meeting held on the 6th Day of October, 2004 by the following vote.

AYES:	COUNCIL MEMBERS:
NOES:	COUNCIL MEMBERS:
ABSTAIN:	COUNCIL MEMBERS:
ABSENT:	COUNCIL MEMBERS:

🏛 CERTIFICATION 🏛

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Resolution No. , adopted by the City Council at a Regular Meeting held on October 6, 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT
MEETING DATE: October 6, 2004

**APPROVAL OF AMENDMENT TO PROFESSIONAL
SERVICES CONTRACT FOR THE BUTTERFIELD BLVD.
NORTH CONNECTION FEASIBILITY STUDY**

RECOMMENDED ACTION: Authorize the City Manager to execute an amendment in the amount of \$11,120 to the City's professional services agreement with **Fehr and Peers** to study alignment and rail crossing alternatives for the northerly segment of Butterfield Blvd.

EXECUTIVE SUMMARY: The Circulation Element of the City's General Plan calls for a special study to evaluate alternatives for connecting Butterfield Blvd. to Monterey Road and for connecting Monterey Road to the Santa Teresa corridor at the north end of the City. At its August 20, 2003 meeting, the City Council authorized the City Manager to execute a professional services agreement with Fehr and Peers to prepare the study for a fee of \$66,824.

The Fehr and Peers study, which is nearly complete, will provide the City with a look at alternatives for establishing a major east-west thoroughfare across the UPRR track at the north end of the City that would connect Butterfield Blvd. with Santa Teresa corridor. The study effort has included the accumulation of traffic counts in the north part of the City, the preparation of traffic forecasts, geometric analysis and plan maps of roadway alternatives, development of grade separation feasibility, and the preparation of rough order of magnitude cost estimates.

Since the study began, several issues have come up that affect the conclusions reached and alternatives analysis. The project manager for Fehr and Peers has submitted a request for additional compensation for work they have performed or recommend that they perform above and beyond the original scope of the agreement. The additional scope involves work required to manipulate the traffic model to ensure reliable forecasting, investigations into the affects of the proposed Coyote Valley Specific Plan, recent PUC actions that could affect this project, property specific construction issues, and a closer look at cost estimates in light of recent inflationary pressures in the construction industry. Staff has reviewed the consultant's request and agrees that an amendment is in order.

FISCAL IMPACT: The proposed study of the Butterfield Blvd. north connection to the Santa Teresa corridor has been budgeted in the current CIP program and is funded by Project No. 501093, Plan Line Major Streets. The City Council has approved an expenditure of \$66,824. The proposed amendment is in the amount of \$11,120. If approved, the amendment will raise the not-to-exceed fee to \$77,944.

Agenda Item # 8

Prepared By:

Deputy Director PW

Approved By:

Department Director

Submitted By:

City Manager



CITY COUNCIL STAFF REPORT
MEETING DATE: OCTOBER 6, 2004

**APPROVAL OF SUBDIVISION IMPROVEMENT
AGREEMENT WITH MORGAN HILL DEVELOPMENT
PARTNERS, L.P. – SUTTER PLACE APN 726-25-012 & 029**

RECOMMENDED ACTION(S): Approve the attached Subdivision Improvement Agreement and authorize the City Manager to sign the agreement on behalf of the City with Morgan Hill Development Partners, L.P., Digital Drive (APN 726-25-012 & 029)

Agenda Item # 9

Prepared By:

Senior Civil Engineer

Approved By:

Public Works Director

Submitted By:

City Manager

EXECUTIVE SUMMARY: In October 2001, Morgan Hill Development Partners entered into a subdivision improvement agreement for their property on the west side of Butterfield Boulevard. The subdivision conditions required the developer to extend Sutter Place from Butterfield Boulevard to Digital Drive. The original subdivision improvement agreement has expired without the completion of the Sutter Place extension. Morgan Hill Ranch Development Partners has requested that they be granted additional time to construct the Sutter Place improvements. The basis of their request is due largely to the present vacancy rate of existing commercial/industrial properties in the area and the lack of interest in developing new commercial/industrial properties.

Staff has reviewed their request and determined that construction of the roadway improvements can be delayed with the installation of a temporary traffic signal at the intersection of Butterfield Boulevard and Digital Drive/South Jarvis Drive. Morgan Hill Ranch Development Partners has agreed to install the temporary traffic signal. The temporary traffic signal will be removed by Morgan Hill Ranch Development Partners upon completion of the Sutter Place improvements

To grant Morgan Hill Development Partners' request for additional time it has been determined that they must enter into a new subdivision improvement agreement with the City. Staff has prepared a new Subdivision Improvement Agreement which will grant Morgan Hill Development Partners two additional years to complete the required improvements. Staff recommends that City Council approve the new Subdivision Improvement Agreement and authorize the City Manager to sign on behalf of the City.

FISCAL IMPACT: Development review for this project is from development processing fees.



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

RECISSION OF WATER SUPPLY EMERGENCY RESOLUTION AND STATUS OF PERCHLORATE REMOVAL PLANTS

RECOMMENDED ACTION(S):

1. Adopt attached resolution ending the water supply emergency; and
2. Accept status report on perchlorate removal plants.

EXECUTIVE SUMMARY: Given the high potential for water shortages this summer that would compromise the City's ability to supply an adequate amount of water for fire safety, the Council adopted a resolution on August 18, 2004 declaring a water supply emergency. With the reactivation of the Tennant Well into the City's water supply system and the lower demand generated by shorter days and cooler weather, the potential for acute water supply shortages has dramatically lowered. Therefore, staff recommends that the Council adopt the attached resolution officially ending the declared water supply emergency.

This item also represents an opportunity to inform the Council about the status of the perchlorate removal plants at the Nordstrom and Tennant wells. The Nordstrom well, which was activated on May 1st of this year has been key to meeting the City's water demand this summer. This well is due to be deactivated on October 31 for the winter months when the well is not needed to meet anticipated demand. The City will spend approximately \$261,000 operating the Nordstrom perchlorate treatment plant this year which is a major cost covered by the Perchlorate Surcharge now added to all City water bills.

The Tennant well is expected to be reactivated on October 1, 2004 after being turned off for over two years. The new perchlorate removal plant at the Tennant well will operate 24 hours per day for the foreseeable future. Funding for the first year of this plant's operation (estimated at \$140,000) is being provided by the Santa Clara Valley Water District.

FISCAL IMPACT: While the operation of the perchlorate removal plants has fiscal implications, no budget adjustment is required by this council item. In accordance with Council direction, staff will continue to seek reimbursement from the Olin Corporation for all perchlorate related expenses.

Agenda Item # 10

Prepared By:

Program Administrator

Approved By:

Public Works Director

Submitted By:

City Manager

RESOLUTION NO.

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL RESCINDING THE DECLARATION OF A WATER SHORTAGE EMERGENCY

WHEREAS, the City of Morgan Hill owns and operates a municipal water system; and,

WHEREAS, this water system draws 100% of its supply from a ground water aquifer;
and,

WHEREAS, the aquifer in and around the City contains perchlorate due to contamination caused by Olin Corporation and Standard Fusee; and,

WHEREAS, the level of contamination has, from time to time, reached Action Levels adopted by the State of California and the Federal Environmental Protection Agency; and,

WHEREAS, when well samplings find perchlorate in the City's water, the City Council may deem it prudent and/or legally necessary to shut off a particular well until well-head treatment is installed, and/or sampling results demonstrate a reduced level of perchlorate; and,

WHEREAS, the City Council found and determined at its meeting on August 18, 2004 that the ordinary demands and requirements of water consumers cannot be satisfied on occasion without depleting the water supply of the City to the extent that there would be insufficient water for human consumption, sanitation, and fire protection; and,

WHEREAS, the City Council duly considered all information presented to it at the duly-noticed public hearing held on August 18, 2004, at which consumers of the City's water supply had an opportunity to be heard to protest against the declaration and present their respective needs; and,

WHEREAS, the City Council found and determined at its meeting on August 18, 2004 that a water supply emergency exists; and,

WHEREAS, the City Council finds and determines that, due to the cooler weather and shorter days experienced in the Fall and Winter months, the ordinary demands and requirements of water consumers can be satisfied without depleting the water supply of the City to the extent that there would be insufficient water for human consumption, sanitation, and fire protection; and,

NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Morgan Hill that the Water Supply Shortage Plan adopted on August 18, 2004 is hereby rescinded.

PASSED AND ADOPTED by the City Council of Morgan Hill at a Regular Meeting held on the 6th Day of October, 2004 by the following vote.

AYES: **COUNCIL MEMBERS:**
NOES: **COUNCIL MEMBERS:**
ABSTAIN: **COUNCIL MEMBERS:**
ABSENT: **COUNCIL MEMBERS:**

☞ CERTIFICATION ☞

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Resolution No. , adopted by the City Council at a Regular Meeting held on October 6, 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item # 11

Prepared By:

Deputy City Clerk

Approved By:

City Clerk

Submitted By:

City Manager

ADOPT ORDINANCE NO. 1695, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM ML, LIGHT INDUSTRIAL TO PLANNED UNIT DEVELOPMENT FOR A 7.72-ACRE PARCEL LOCATED AT THE NORTHWEST CORNER OF COCHRANE ROAD AND MADRONE PARKWAY IN THE MADRONE BUSINESS PARK (APN 726-33-028) (ZA-04-11: COCHRANE - TBI)

RECOMMENDED ACTION(S):

Waive the Reading, and **Adopt** Ordinance No. 1695, New Series, As Amended, and **Declare** That Said Title, Which Appears on the Public Agenda, Shall Be Determined to Have Been Read by Title and Further Reading Waived.

EXECUTIVE SUMMARY:

At a Regular City Council meeting on September 15, 2004, the City Council Introduced Ordinance No. 1695, New Series, with an amended Exhibit B, by the Following Roll Call Vote: AYES: Carr, Chang, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: None.

FISCAL IMPACT:

None. Filing fees were paid to the City to cover the cost of processing this application.

ORDINANCE NO. 1695, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM ML, LIGHT INDUSTRIAL TO PLANNED UNIT DEVELOPMENT FOR A 7.72-ACRE PARCEL LOCATED AT THE NORTHWEST CORNER OF COCHRANE ROAD AND MADRONE PARKWAY IN THE MADRONE BUSINESS PARK (APN 726-33-028)(ZA-04-11: COCHRANE - TBI)

THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY ORDAIN AS FOLLOWS:

- SECTION 1.** The proposed zoning amendment is consistent with the Zoning Ordinance and the General Plan.
- SECTION 2.** The zone change is required in order to serve the public convenience, necessity and general welfare as provided in Section 18.62.050 of the Municipal Code.
- SECTION 3.** An environmental initial study has been prepared for this application and has been found complete, correct and in substantial compliance with the requirements of California Environmental Quality Act. A mitigated Negative Declaration will be filed.
- SECTION 4.** The City Council hereby approves an amendment to the zoning designation from ML, Light Industrial to Planned Unit Development for a 7.72-acre parcel, as shown on the attached zoning plat (Exhibit A).
- SECTION 5.** Prior to an application for any further entitlement, the property owner shall obtain approval of a precise development plan for the subject property. A precise development plan and PUD Guidelines are not required at this time as future uses have not yet been identified. Creating a PUD overlay zoning district will enhance the marketability of the site to attract the most desirable uses for the City.
- SECTION 6.** Future development of the 7.72-acre site shall comply with the development standards of Chapter 18.30, PUD Planned Unit Development District, of the Morgan Hill Municipal Code in effect at time of project approval.
- SECTION 7.** Future development of the 7.72-acre site shall comply with the mitigation measures of the approved mitigated Negative Declaration. Should future uses be proposed that would generate vehicle trips beyond what was analyzed in the project traffic study, a supplemental traffic analysis shall be required.

SECTION 8. Permitted uses within the PUD shall be supportive of the neighboring industrial business parks and compatible with the surrounding built environment, as identified in the attached Exhibit B.

SECTION 9. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 10. Effective Date; Publication. This Ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

The foregoing ordinance was introduced at the regular meeting of the City Council of the City of Morgan Hill held on the 15th Day of September 2004, and was finally adopted at a regular meeting of said Council on the 6th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: COUNCIL MEMBERS:
NOES: COUNCIL MEMBERS:
ABSTAIN: COUNCIL MEMBERS:
ABSENT: COUNCIL MEMBERS:

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

⌘ CERTIFICATE OF THE CITY CLERK ⌘

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. 1695, New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the 6th Day of October 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk

EXHIBIT B
NEW MADRONE PLANNED UNIT DEVELOPMENT

Permitted Uses

- Retail Stores
- Restaurants
- Offices and Professional Offices (excluding medical, dental and/or health related offices)
- Financial Services
- Personal Services
- Business and Trade Schools
- Specialty Grocery Stores, not to exceed 15,000 sf
- Drug Stores

Conditional Uses

- Day Care Centers/Nursery Schools
- Commercial Recreation
- Gasoline Service Stations (including ancillary convenience stores)
- Drive-thru uses
- Grocery Stores exceeding 15,000 sf but less than 50,000 sf
- Any other use which the Planning Commission finds to be of similar nature to the permitted uses and conditional uses specified above



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item # 12

Prepared By:

Deputy City Clerk

Approved By:

City Clerk

Submitted By:

City Manager

ADOPT ORDINANCE NO. 1696, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM PUD, RESEARCH AND DEVELOPMENT/ MANUFACTURING TO PUD, R3 MEDIUM DENSITY RESIDENTIAL FOR TWO PARCELS TOTALING 15.78 ACRES IN SIZE, LOCATED AT THE SOUTHEAST CORNER OF COCHRANE ROAD AND MONTEREY ROAD IN THE MORGAN HILL RANCH BUSINESS PARK (APNs 726-25-076 & - 077)(ZA-04-09: BUTTERFIELD – SOUTH VALLEY DEVELOPERS)

RECOMMENDED ACTION(S):

Waive the Reading, and **Adopt** Ordinance No. 1696, New Series, and **Declare** That Said Title, Which Appears on the Public Agenda, Shall Be Determined to Have Been Read by Title and Further Reading Waived.

EXECUTIVE SUMMARY:

At a Regular City Council meeting on September 15, 2004, the City Council Introduced Ordinance No. 1696, New Series, by the Following Roll Call Vote: AYES: Carr, Chang, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: None.

FISCAL IMPACT:

None. Filing fees were paid to the City to cover the cost of processing this application.

ORDINANCE NO. 1696, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM PUD, RESEARCH AND DEVELOPMENT/MANUFACTURING TO PUD, R3 MEDIUM DENSITY RESIDENTIAL FOR TWO PARCELS TOTALING 15.78 ACRES IN SIZE, LOCATED AT THE SOUTHEAST CORNER OF COCHRANE ROAD AND MONTEREY ROAD IN THE MORGAN HILL RANCH BUSINESS PARK (APNs 726-25-076 & -077) (ZA-04-09: BUTTERFIELD – SOUTH VALLEY DEVELOPERS)

THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY ORDAIN AS FOLLOWS:

- SECTION 1.** The proposed zoning amendment is consistent with the Zoning Ordinance and the General Plan.
- SECTION 2.** The zone change is required in order to serve the public convenience, necessity and general welfare as provided in Section 18.62.050 of the Municipal Code.
- SECTION 3.** An environmental initial study has been prepared for this application and has been found complete, correct and in substantial compliance with the requirements of California Environmental Quality Act. A mitigated Negative Declaration will be filed.
- SECTION 4.** The City Council hereby approves an amendment to the zoning designation from PUD, Research and Development/Manufacturing to PUD, R3 Medium Density Residential for two parcels totaling 15.78 acres in size, as shown on the attached zoning plat (Exhibit A).
- SECTION 5.** Prior to development of the 15.78-acre site, the project applicant shall first secure building allotments under the Residential Development Control System for the number of units proposed in the development.
- SECTION 6.** Future development of the 15.78-acre site shall comply with the site development standards of the R3, Medium Density Residential District in effect at time of project approval, unless otherwise approved as part of a Residential Planned Development.
- SECTION 7.** Future development of the 15.78-acre site shall comply with the mitigation measures of the approved mitigated Negative Declaration.

SECTION 8. The applicant shall cure all defaults of any subdivision improvement agreement; development agreement, including but not limited to payment of assessments, penalties and interest; and/or any other agreements between the applicant and the City of Morgan Hill prior to the award and distribution of Measure C building allotments.

SECTION 9. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 10. Effective Date; Publication. This Ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

The foregoing ordinance was introduced at the regular meeting of the City Council of the City of Morgan Hill held on the 15th Day of September 2004, and was finally adopted at a regular meeting of said Council on the 6th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: COUNCIL MEMBERS:
NOES: COUNCIL MEMBERS:
ABSTAIN: COUNCIL MEMBERS:
ABSENT: COUNCIL MEMBERS:

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

⌘ CERTIFICATE OF THE CITY CLERK ⌘

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. 1696, New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the 6th Day of October 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item # 13

Prepared By:

Deputy City Clerk

Approved By:

City Clerk

Submitted By:

City Manager

ADOPT ORDINANCE NO. 1697, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A SET OF DEVELOPMENT STANDARDS AND ARCHITECTURAL GUIDE LINES FOR THE DE PAUL (FORMERLY SAINT LOUISE) HEALTH CENTER. (APNs 728-031-005, 006, 012 & 013)

RECOMMENDED ACTION(S):

Waive the Reading, and **Adopt** Ordinance No. 1697, New Series, and **Declare** That Said Title, Which Appears on the Public Agenda, Shall Be Determined to Have Been Read by Title and Further Reading Waived.

EXECUTIVE SUMMARY:

At a Regular City Council meeting on September 15, 2004, the City Council Introduced Ordinance No. 1697, New Series, by the Following Roll Call Vote: AYES: Carr, Chang, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: None.

FISCAL IMPACT:

No budget adjustment required.

ORDINANCE NO. 1697, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A SET OF DEVELOPMENT STANDARDS AND ARCHITECTURAL GUIDE LINES FOR THE DE PAUL (FORMERLY SAINT LOUISE) HEALTH CENTER. (APNs 728-031-005, 006, 012 & 013)

THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY ORDAIN AS FOLLOWS:

- SECTION 1.** AMENDING THE PLANNED UNIT DEVELOPMENT ZONING DISTRICT. This ordinance here by amends the precise development plan established under Ordinance No. 1689, New Series. The amendment is limited to the addition of the Design Standards and Architectural Guidelines attached hereto as Exhibit A and Exhibit B.
- SECTION 2.** The incorporation of the design standards and architectural guidelines is consistent with the Zoning Ordinance and the General Plan since these standards and guidelines further define the DePaul precise development plan adopted under Ordinance No. 1689.
- SECTION 3.** The zoning amendment is required in order to serve the public convenience, necessity and general welfare as provided in Section 18.62.050 of the Municipal Code and to fulfill the design requirements within Section 18.30.050 of the Municipal Code .
- SECTION 4.** An environmental assessment has been prepared for the zoning amendment and is deemed complete, correct and adequate in accordance with state and local environmental guidelines. Based upon said study, a Mitigated Negative Declaration has been filed.
- SECTION 5.** The City Council finds that the proposed amendment of the Planned Unit Development Overlay District is consistent with the criteria specified in Chapter 18.30 of the Morgan Hill Municipal Code.
- SECTION 6.** The City Council hereby approves of the Design Standards dated July 1, 2004, on file in the Community Development Department, entitled, "Design Standards, De Paul Planned Unit Development (PUD)" as shown on the attached Exhibit A.
- SECTION 7.** The City Council hereby approves of the Architectural Guidelines standard dated August 26, 2004, on file in the Community Development Department, entitled, "De Paul Planned Unit Development (PUD) Architectural Design Guidelines" as shown on the attached Exhibit B.

SECTION 8. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 9. Effective Date; Publication. This Ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

The foregoing ordinance was introduced at the regular meeting of the City Council of the City of Morgan Hill held on the 15th Day of September 2004, and was finally adopted at a regular meeting of said Council on the 6th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: COUNCIL MEMBERS:
NOES: COUNCIL MEMBERS:
ABSTAIN: COUNCIL MEMBERS:
ABSENT: COUNCIL MEMBERS:

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

∞ CERTIFICATE OF THE CITY CLERK ∞

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. 1697, New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the 6th Day of October 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk

ORDINANCE NO. 1697, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A SET OF DEVELOPMENT STANDARDS AND ARCHITECTURAL GUIDE LINES FOR THE DE PAUL (FORMERLY SAINT LOUISE) HEALTH CENTER. (APNs 728-031-005, 006, 012 & 013)

THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY ORDAIN AS FOLLOWS:

- SECTION 1.** AMENDING THE PLANNED UNIT DEVELOPMENT ZONING DISTRICT. This ordinance here by amends the precise development plan established under Ordinance No. 1689, New Series. The amendment is limited to the addition of the Design Standards and Architectural Guidelines attached hereto as Exhibit A and Exhibit B.
- SECTION 2.** The incorporation of the design standards and architectural guidelines is consistent with the Zoning Ordinance and the General Plan since these standards and guidelines further define the DePaul precise development plan adopted under Ordinance No. 1689.
- SECTION 3.** The zoning amendment is required in order to serve the public convenience, necessity and general welfare as provided in Section 18.62.050 of the Municipal Code and to fulfill the design requirements within Section 18.30.050 of the Municipal Code .
- SECTION 4.** An environmental assessment has been prepared for the zoning amendment and is deemed complete, correct and adequate in accordance with state and local environmental guidelines. Based upon said study, a Mitigated Negative Declaration has been filed.
- SECTION 5.** The City Council finds that the proposed amendment of the Planned Unit Development Overlay District is consistent with the criteria specified in Chapter 18.30 of the Morgan Hill Municipal Code.
- SECTION 6.** The City Council hereby approves of the Design Standards dated July 1, 2004, on file in the Community Development Department, entitled, "Design Standards, De Paul Planned Unit Development (PUD)" as shown on the attached Exhibit A.
- SECTION 7.** The City Council hereby approves of the Architectural Guidelines standard dated August 26, 2004, on file in the Community Development Department, entitled, "De Paul Planned Unit Development (PUD) Architectural Design Guidelines" as shown on the attached Exhibit B.

SECTION 8. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 9. Effective Date; Publication. This Ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

The foregoing ordinance was introduced at the regular meeting of the City Council of the City of Morgan Hill held on the 15th Day of September 2004, and was finally adopted at a regular meeting of said Council on the 6th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: COUNCIL MEMBERS:
NOES: COUNCIL MEMBERS:
ABSTAIN: COUNCIL MEMBERS:
ABSENT: COUNCIL MEMBERS:

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

∞ CERTIFICATE OF THE CITY CLERK ∞

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. 1697, New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the 6th Day of October 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item # 14

Prepared By:

Deputy City Clerk

Approved By:

City Clerk

Submitted By:

City Manager

ADOPT ORDINANCE NO. 1698, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A DEVELOPMENT AGREEMENT WITH DAN GAMEL, INC. FOR THE EXPANSION OF DAN GAMEL'S MORGAN HILL RECREATIONAL VEHICLE (RV) CENTER

RECOMMENDED ACTION(S):

Waive the Reading, and **Adopt** Ordinance No. 1698, New Series, and **Declare** That Said Title, Which Appears on the Public Agenda, Shall Be Determined to Have Been Read by Title and Further Reading Waived.

EXECUTIVE SUMMARY:

At a Special Meeting on September 22, 2004, the City Council Introduced Ordinance No. 1698, New Series, by the Following Roll Call Vote: AYES: Carr, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: Chang.

FISCAL IMPACT:

The City will experience a net gain of revenue when one takes into account the loss of revenue if Gamel RV had left town or when compared to the previous sales tax sharing agreement with Gamel RV that recently expired.

ORDINANCE NO. 1698, NEW SERIES

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A DEVELOPMENT AGREEMENT WITH DAN GAMEL, INC. FOR THE EXPANSION OF DAN GAMEL'S MORGAN HILL RECREATIONAL VEHICLE (RV) CENTER

WHEREAS, California Government Code Sections 65864 through 65869.5 authorizes the City of Morgan Hill to enter into binding development agreements with persons having legal or equitable interests in real property for the development of such property; and

WHEREAS, the City Council has duly considered the Development Agreement between the City and Dan Gamel, Inc. ("Agreement"), which is incorporated herein by reference and which sets forth in detail the specific responsibilities of the City and Dan Gamel, Inc. regarding the development of the subject property.

WHEREAS, the said Agreement shall be binding on all future owners and developers as well as the present owners of the lands, and any substantial change in the Agreement may be made only after further public hearings before the Planning Commission and the City Council of this City;

WHEREAS, the City Council therefore finds that the development proposal and agreement approved by this ordinance are compatible with the goals, objectives, policies, and land uses designated by the General Plan of the City of Morgan Hill; and

WHEREAS, the Council finds that the Agreement serves the general health, safety and welfare interests of the citizens of Morgan Hill as stated with more particularly in the Agreement.

NOW, THEREFORE, the City Council of the City of Morgan Hill, California does ordain as follows:

SECTION 1. Based upon the foregoing findings, the Agreement is hereby approved.

SECTION 2. Authority is hereby granted to the City Manager to execute the agreement approved by the City Council during the Public Hearing Process, and any documents necessary and appropriate to effectuate the terms of the Agreement.

SECTION 3. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 4. Effective Date; Publication. This Ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

The foregoing ordinance was introduced at the Special meeting of the City Council of the City of Morgan Hill held on the 22nd Day of September 2004, and was finally adopted at a regular meeting of said Council on the 6th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: COUNCIL MEMBERS:
NOES: COUNCIL MEMBERS:
ABSTAIN: COUNCIL MEMBERS:
ABSENT: COUNCIL MEMBERS:

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

∞ CERTIFICATE OF THE CITY CLERK ∞

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. 1698, New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the 6th Day of October 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT

MEETING DATE: OCTOBER 6, 2004

TITLE: RE-BUDGETING 03/04 PROJECTS/PROGRAMS

RECOMMENDED ACTION(S):

- 1) Approve the re-budgeting of 03/04 project/program costs in the 04/05 budget.

EXECUTIVE SUMMARY:

Certain project and programs costs for various funds were projected as being completed before the end of the 2003/04 fiscal year and were not budgeted in 2004/05. A budget amendment is needed to re-budget in 2004/05 for those projects/programs that were not completed at the end of 03/04.

FISCAL IMPACT:

The amounts for re-budgeting in fiscal year 2004/05 have no impact on fund balance. These costs were expected to be spent in fiscal year 03/04 and were included in projected expenditures at year end and used in calculating ending fund balance. A summary of the projects/programs being re-budgeted with unspent 03/04 appropriations is attached (Exhibit A). Please note that negative re-budgets typically result from higher than year-end projected expenditures in the prior year.

Agenda Item # 1

Prepared By:

Budget Manager

Approved By:

Finance Director

Submitted By:

City Manager

FY03/04 Rebudget to FY04/05

Account	Capital Project Description	Total
202-86360-8050-528001	Monterey/UPRR Ped Acces & Bike Path	\$ 238,996
	Street Maintenace Fund Total	238,996
232-86360-5800-519096	Pavement Rehabilitation Program	100,000
	Environmental Programs Fund Total	100,000
301-86360-8051-118001	Paradise Park Play Equipment	37,998
	Park Development Fund Total	37,998
309-86360-8053-501###	Plan Line Major Streets	62,386
309-86360-8053-502###	New Signal Construction	349,249
309-86360-8053-507B99	Tennant Ave Widening	114,919
	Traffic Impact Fund Total	526,553
311-86360-8080-228000	Police Facility	(493)
	Police Impact Fund Total	(493)
313-86360-8085-231003	Fire Station (Purchase CalTrain property)	22,195
	Fire Impact Fund Total	22,195
317-86360-8055-114000	Regional Soccer Complex	8,153
317-86360-8055-115000	Aquatics Center	635,024
317-86360-8055-228000	Police Facility	1,699,672
317-86360-8055-229001	Indoor Recreation Center	(889,301)
317-86360-8055-507B99	Tennant Ave Widening	623,469
317-86360-8055-519096	Pavement Rehabilitation Program	347,162
317-86360-8055-519J03	Street Resurface 02/03	100,148
317-86360-8055-519L04	Slurry Seal Project	(20,043)
	RDA Fund Total	2,504,283
346-86360-8049-115000	Aquatics Center	187,000
346-86360-8049-228000	Police Facility	6,146,201
	Public Facil. (Non AB1600) Fund Total	6,333,201
350-86360-8057-529001	Underground Misc Locations	33,750
	Undergrounding Fund Total	33,750
641-86360-8140-308094	Sewer Trunk Line	329,887
	Sewer Impact Fund Total	329,887
643-86360-8170-302###	Sanitary Sewer Rehabilitation	252,438
643-86360-8170-304###	Lift Station Improvements	274,757
643-86360-8170-305093	Lift Station Telemetry	3,380
	Sewer CIP Fund Total	530,576
651-86360-8110-601###	New Well Property/Construction	(79,349)
651-86360-8110-602###	New Water Reservoirs	841,564
651-86360-8110-603093	New Water Mains	120,000
651-86360-8110-619002	Edmundson Main Distribution	414,727
	Water Impact Fund Total	1,296,942
653-86360-8120-601###	New Well Property/Construction	331,418
653-86360-8120-602###	New Water Reservoirs	882,511
653-86360-8120-606093	Radio Telemetry	17,726
653-86360-8120-610###	Water Main Replacement	196,422
	Water CIP Fund Total	1,428,077
	Total CIP Projects	\$ 13,381,966

Account	Oprations Project Description	Total
215-86440-8000	CDBG Programs	\$ 214,299
	HCD Fund Total	214,299
216-86420-8001-HCD984	Various CDBG Housing Loans	102,241
	HCD Rehab Fund Total	102,241
317-42231-7000	RDA Financing Plan	20,000
317-82231-8010	CRPO Update	25,000
317-82231-8010	Monterey Traffic Study	90,000
317-86340-8010	TI for Train Depot Building	30,000
317-86420-8010-RDA085	Granary & Misc. Loan Programs	125,000
317-86420-8010-RDA095	Scoffone Loan	150,000
317-86440-8010-RDA018	Facade Improvement Program	295,825
	RDA Fund Total	735,825
327-86441-7100-RDA080	Watsonville Road Housing Program	743,091
	Housing Fund Total	743,091
	Total Operations Projects	\$ 1,795,457

**CITY OF MORGAN HILL
JOINT SPECIAL AND REGULAR CITY COUNCIL
AND SPECIAL REDEVELOPMENT AGENCY MEETING
MINUTES – SEPTEMBER 15, 2004**

CALL TO ORDER

Mayor/Chairman Kennedy called the special meeting to order at 6:01 p.m.

ROLL CALL ATTENDANCE

Present: Council/Agency Members Carr, Tate and Mayor/Chairman Kennedy
Late: Mayor Pro Tempore/Vice-chair Sellers (arrived at 6:30 p.m.) and Council/Agency Member Chang (arrived at 7:08 p.m.)

DECLARATION OF POSTING OF AGENDA

City Clerk/Agency Secretary Torrez certified that the meeting's agenda was duly noticed and posted in accordance with Government Code 54954.2.

City Council and Redevelopment Agency Action

CLOSED SESSIONS:

Mayor/Chairman Kennedy announced the following closed session items:

1.

CONFERENCE WITH LEGAL COUNSEL - ANTICIPATED LITIGATION

Authority: Government Code Sections 54956.9(b) & (c)
Number of Potential Cases: 4

2.

PUBLIC EMPLOYEE PERFORMANCE EVALUATION

Authority: Government Code 54957
Public Employee Performance Evaluation: City Manager
Attendees: City Council

3.

CONFERENCE WITH LEGAL COUNSEL - EXISTING LITIGATION:

Authority: Pursuant to Government Code 54956.9(a)
Case Name: General Lighting Service, Inc. v. City of Morgan Hill
Case Number: Santa Clara County Superior Court, Case No. 1-04-CV-025561

4.

PUBLIC EMPLOYEE PERFORMANCE EVALUATION

Legal Authority: Government Code 54957
Public Employee Performance Evaluation: City Attorney
Attendees: City Council, City Attorney

Council/Agency Member Chang was not present during closed session discussions.

OPPORTUNITY FOR PUBLIC COMMENT

Mayor/Chairman Kennedy opened the Closed Session items to public comment. No comments were offered.

ADJOURN TO CLOSED SESSION

Mayor/Chairman Kennedy adjourned the meeting to Closed Session at 6:03 p.m.

RECONVENE

Mayor/Chairman Kennedy reconvened the meeting at 7:07 p.m.

Council/Agency Member Chang entered and took her seat on the Dias.

CLOSED SESSION ANNOUNCEMENT

Mayor/Chairman Kennedy announced that the closed session items were continued to the conclusion of the open session meeting.

SILENT INVOCATION

PLEDGE OF ALLEGIANCE

PROCLAMATIONS

Mayor Kennedy presented a proclamation to Nathalie Averett, National Society of the Daughters of the American Revolution, declaring the week of September 17-23, 2004 as *Constitution Week*.

RECOGNITIONS

Programs Administrator Eulo and Mayor Kennedy distributed Certificates of Recognition to honor the following Water Heroes: Jody Barcellos, Comcast Cable; Connie Ibost, Anritsu Corporation; Peter McKenna, Morgan Hill Unified School District; Intercon Technology; Alien Technology; South Valley Developers, and Cochrane Plaza.

CITY COUNCIL REPORT

Mayor Pro Tempore Sellers reported on the following: 1) The Downtown Association is very active following receipt of seed money from the City toward becoming an independent organization. One of the productive ways to become independent is to start a Property Based Improvement District (PBID). This will allow businesses in the community to fund themselves and provide resources for their own benefit, determining how to best use these funds. At the last Council meeting, the Downtown

Association requested that the City help with the money required to undertake this process. He indicated that this is an involved process and involves two different votes, surveys and background work to figure out how much individuals should be assessed. He indicated that the Downtown Association met this morning and that it is well underway toward the PBID process. 2) He indicated that an election will be held on November 2, 2004. He felt that individuals involved in the election process have a duty to uphold the highest standard. He stated that he and Mayor Kennedy are determined to have a code of conduct and to conduct themselves in a way that is exemplary. He urged all Council and School Board candidates to do the same. He felt that how an individual campaigns is a good indication of how one will govern and serve.

Council Member Chang announced that the South County Wastewater Regional Authority (SCWRA) Board received its river discharge permit last Friday following a 20-year effort.

CITY MANAGER REPORT

City Manager Tewes indicated that at the last meeting, the Council received a report from the Legislative Subcommittee who indicated that they would be reviewing all state propositions. The Legislative Subcommittee recommended that the City begin an analysis of Proposition 1A, the proposition that will provide constitutional protection for local City revenues so that the revenues can be applied to local services rather than being diverted to the State. He informed the Council that the Finance & Audit Committee will be reviewing Proposition 1A at their upcoming meeting.

CITY ATTORNEY REPORT

Acting City Attorney McClure stated that he did not have a City Attorney's report to present this evening.

OTHER REPORTS

None.

PUBLIC COMMENT

Mayor/Chairman Kennedy opened the floor to public comments for items not appearing on this evening's agenda.

A Live Oak High School student requested clarification on the comment expressed by Council Member Chang.

Mayor Kennedy explained that the City shares a wastewater treatment plant with the City of Gilroy and that the facility is located in Gilroy. The treated wastewater is disposed by percolation. However, in the winter time, when it rains a lot, the percolation ponds fill up. SCRWA applied for a permit in order to discharge tertiary treated water into the Llagas Creek and Pajaro River. He indicated that SCRWA was

successful in getting the permit approved; allowing the highly treated, purified water to be released into the Pajaro River.

No further comments were offered.

City Council Action

CONSENT CALENDAR:

Mayor Pro Tempore Sellers requested that item 2 be removed from the consent calendar to ask a question and Council/Agency Member Chang requested that item 12 be removed from the Consent Calendar as she would be abstaining from voting on the minutes as she was not in attendance of the meetings held on September 1, 2004.

Action: *On a motion by Mayor Pro Tempore Sellers and seconded by Council Member Tate, the City Council unanimously (5-0) **Approved** Consent Calendar Items 1, 3-11 and 13 as follows:*

1. **AGREEMENT WITH THE LAW FIRM OF HATCH & PARENT**

Action: **Authorized** *the City Manager to Execute an Agreement with the Law Firm of Hatch & Parent.*

3. **AMENDMENT TO AGREEMENT WITH SANTA CLARA VALLEY WATER DISTRICT REGARDING THE OPERATION OF THE TENNANT WELL PERCHLORATE REMOVAL SYSTEM**

Action: **Authorized** *the City Manager to Execute an Amendment to the Existing Agreement with Santa Clara Valley Water District for the Operation of Tennant Well, Subject to Review and Approval by the City Attorney.*

4. **APPROVAL OF IMPROVEMENT AGREEMENT FOR 18585 MONTEREY ROAD – GATEWAY CENTER, PHASE 2 (APN: 764-10-009)**

Action: **Approved** *the Improvement Agreement with South Valley Developers, Inc. and 2) **Authorized** the City Manager to Sign the Agreement on Behalf of the City.*

5. **ACCEPTANCE OF SUBDIVISION IMPROVEMENTS FOR TRACT 8791, DEL MONTE ESTATES**

Action: 1) **Adopted** *Resolution No. 5841, Accepting the Subdivision Improvements Included in Tract 8791, Commonly Known as Del Monte Estates; and 2) **Directed** the City Clerk to File a Notice of Completion with the County Recorder's Office.*

6. **ACCEPTANCE OF SUBDIVISION IMPROVEMENTS FOR QUAIL CREEK PHASE I (TRACT 9427)**

Action: 1) **Adopted** Resolution No. 5842, Accepting the Subdivision Improvements Included in Tract 9427, Commonly Known as Quail Creek, Phase I; and 2) **Directed** the City Clerk to File a Notice of Completion with the County Recorder's Office.

7. **FINAL MAP APPROVAL FOR QUAIL CREEK, PHASE III (TRACT 9561)**

Action: 1) **Approved** the Final Map, Subdivision Agreement, and Improvement Plans; 2) **Authorized** the City Manager to Sign the Subdivision Improvement Agreement on Behalf of the City; and 3) **Authorized** the Recordation of the Map and the Subdivision Improvement Agreement Following Recordation of the Development Improvement Agreement.

8. **AMENDED IMPROVEMENT AGREEMENT FOR 1295 EAST DUNNE AVENUE (APN 728-17-023)**

Action: 1) **Approved** the Amended Improvement Agreement with Mr. and Mrs. Waiyan and Tsai-pi Ho; and 2) **Authorized** the City Manager to Sign the Agreement on Behalf of the City.

9. **RESOLUTION REQUESTING AUTHORIZATION UNDER SECTION 21221(h) OF CALIFORNIA CODE FROM PUBLIC EMPLOYEES RETIREMENT SYSTEM (CalPERS) FOR BRUCE CUMMING TO BE EMPLOYED FOR MORE THAN 960 HOURS IN A ONE-YEAR PERIOD**

Action: **Approved** Resolution No. 5843, Requesting CalPERS for an Extension for Interim Police Chief Bruce Cumming to be Employed for more than 960 Hours in a One-Year Period.

10. **ADOPT ORDINANCE NO. 1694, NEW SERIES**

Action: **Waived** the Reading, and **Adopted** Ordinance No. 1694, New Series, and **Declared** That Said Title, Which Appears on the Public Agenda, Shall be Determined to Have Been Read by Title and Further Reading Waived; Title as Follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING AN AMENDMENT TO ORDINANCE NO. 1474, New Series, AMENDING THE LIST OF PERMITTED USES FOR DIGITAL ISLAND OF THE MORGAN HILL RANCH BUSINESS PARK TO ALLOW GENERAL OFFICE USES AND UP TO 40,000 SQUARE FEET OF MEDICAL/DENTAL OFFICE USES (APNs 726-25-080 thru -082) (ZA-04-07: DIGITAL – VENTURE PROFESSIONAL CENTER).**

11. **SPECIAL CITY COUNCIL MEETING MINUTES FOR AUGUST 11, 2004**

Action: **Approved** the Minutes as Written.

13. **APPOINTMENTS TO THE SANTA CLARA VALLEY TRANSPORTATION AUTHORITY (VTA) VALLEY TRANSPORTATION PLAN DESIGN ENHANCEMENTS (VTP DE) COMMITTEE**

Action: 1) **Appointed** Planning Commissioner Robert Benich, and Architectural Review Board Members James Fruit and Yarmila Kennett to the VTP DE Committee; and 2) **Directed** the City Clerk's Office to Notify the VTA of the City Council's Appointments to this Committee.

2. INFORMATION TECHNOLOGY SERVICES CONTRACT

Mayor Pro Tempore Sellers noted that the City is in the process of contracting with a new vendor to provide information technology services (e.g., computer services and support). He said that one of the items contained in the contract states an interest of having this be a long term contract with a 2-3 year extension. He said that the reason for doing so is that once you bring someone on board, they gain institutional knowledge and you want to keep them on board because they know the City's system. As the City is changing vendors at this time, he suggested that staff discuss a way to overlap the institutional knowledge in the transition with the previous vendor.

Programs Manager Eulo agreed that there is a loss of institutional memory whenever you have a change similar to this or a change in staffing in an organization. He said that in order to counteract the loss and minimize the amount of institutional knowledge that would be lost, the City will employ two strategies: 1) staff for the new contractor will be on site with the staff of the existing contractor for approximately 1.5 weeks; and 2) the new contractor is able to engage the services of the former contractor on a fee for service basis when an onsite assistance is needed.

Action: *On a motion by Mayor Pro Tempore Sellers and seconded by Council Member Tate, the City Council unanimously (5-0) **Authorized** the City Manager to Execute the Agreement, Subject to Review and Approval by the City Attorney.*

12. SPECIAL CITY COUNCIL MEETING MINUTES FOR SEPTEMBER 1, 2004

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council, on a 4-0-1 vote with Council Member Chang abstaining, **Approved** the Minutes as Written.*

City Council and Redevelopment Agency Action

CONSENT CALENDAR:

Council/Agency Member Chang requested that item 14 be removed from the Consent Calendar as she would be abstaining from voting on the item.

14. SPECIAL AND REGULAR CITY COUNCIL AND SPECIAL REDEVELOPMENT AGENCY MEETING MINUTES FOR SEPTEMBER 1, 2004.

Action: *On a motion by Council/Agency Member Tate and seconded by Mayor Pro Tempore/Vice-chair Sellers, the City Council/Agency Board, on a 4-0-1 vote with Council/Agency Member Chang abstaining, **Approved** the Minutes as Written.*

City Council Action

PUBLIC HEARINGS:

15. STREET NAME CHANGE: SAINT LOUISE DRIVE TO DePAUL DRIVE – *Resolution No. 5844*

Planning Manager Rowe presented the staff report, informing the Council that staff provided notification to all of the property owners affected by the street name. He indicated that as of this evening, staff has not received objections to the street name change. Staff concurs with the name change from St. Louise Drive to DePaul Drive as it would eliminate the confusion associated with the same name of the medical facility at another location. Further, the street name change is consistent with the street name policy, that of a mission theme.

Mayor Kennedy opened the public hearing. No comments being offered, the public hearing was closed.

Action: *On a motion by Council Member Tate and seconded by Council Member Carr, the City Council unanimously (5-0) Adopted Resolution No. 5844, Approving the Street Name Change.*

16. GENERAL PLAN AMENDMENT, GPA-04-05/ZONING AMENDMENT, ZA-04-11: COCHRANE-TBI Ordinance No. 1695, New Series & Resolution No. 5845

Planning Manager Rowe presented the staff report, indicating that this is a request to change the general plan land use designation from industrial to commercial and to rezone the property to planned unit development. He stated that the proposed planned unit development includes a variety of commercial uses, including but not limited to a grocery store, drug store, retail uses, restaurants and offices. He said that the Planning Commission reviewed the applications on two occasions in August, addressing the traffic mitigation and the list of uses. The Planning Commission discussed the fact that the proposed amendment would reduce the amount of industrial land in the City. However, the benefit from going to the commercial designation would be to incorporate some business uses that would help serve the surrounding business parks and the community, as a whole, including sales tax revenue to the city. He informed the Council that staff recommended that the PUD be limited to uses supportive of the industrial park that would exclude a grocery store and drugstore. Staff further recommended that the medical, dental, and health related services be excluded from the permitted uses; and that daycare, nursery schools and commercial uses be required as conditional uses. He stated that General Plan Policy 9G, the action statement, indicates that the City should amend the zoning ordinance, as necessary, to preserve a site east of Highway 101 and north of Cochrane Road for a grocery store. He stated that restricting a grocery and drug store in this location would be more consistent with the general plan. If such uses were located in this area, it would tend to make it difficult to locate the uses on the east side of the Freeway. He indicated that the City currently has an application in the process that would implement the action item to accommodate a site for a grocery store east of Highway 101.

Mr. Rowe informed the Council that the applicant is requesting that the exclusion only pertain to medical, dental and/or health related offices as opposed to services. He indicated that the Planning Commission still feels that these types of uses can be considered on a case-by-case basis as part of a conditional use. The applicant is also requesting to include drugstores, wine tasting, and arts & crafts galleries. Under conditional uses, the applicant is requesting to include service stations, including

ancillary convenience stores, and to allow grocery stores exceeding 15,000 square feet as conditional uses.

Mr. Rowe informed the Council that the recommended uses are those that he outlined previously. Staff recommends approval of the mitigated negative declaration, the general plan amendment resolution and introduction of the ordinance that would list the permitted uses as outlined in Exhibit B to the zoning amendment ordinance.

Mayor Kennedy opened the public hearing.

Dan Amend, vice-president of Toeniskoetter and Breeding, Inc. (TBI), pointed out that he worked through the traffic impact of this property at the Planning Commission level. He indicated that the project itself does not create any traffic impacts that would need to be mitigated. However, the General Plan 2025 level of impacts requires some right of ways that TBI will be giving to the City as a part of the project. He requested that the Council approve TBI's request with the use revision as submitted.

Brad Krouskup, TBI, stated that in May 1997, working with the Madrone Land Corporation, approached the owners of the San Jose Trap and Skeet Club with an idea on how to transform the northern side of Cochrane Road and Highway 101. He stated that TBI is proud of the transformation that has taken place, bringing in some successful businesses into town. TBI has a successful project that still is in the works and that they want to continue to be a great neighbor in Morgan Hill. TBI believes that there is an opportunity to create a retail site in the front of the park that can be highly successful. When the park was first envisioned, there was approximately four acres of general commercial retail that fronted Monterey Road. TBI did not believe that this was an important place for retail for the Madrone Business Park and the greater Cochrane Road area. He stated that when TBI had the opportunity to change the zoning designation, they did so in order to bring Paramit Corporation to Morgan Hill.

Mr. Krouskup informed the Council that TBI always envisioned the need for a retail component in the Business Park. He stated that what TBI is proposing can co-exist with other retail that is being proposed for Cochrane Road. He indicated that TBI is aware of the application that is being processed and that TBI wants this project to be a great success. He said that TBI believes that there are three markets that need to be served. He appreciated staff's support of the project as a retail project and the Planning Commission's suggestions. It was his belief that this retail site has a great opportunity to serve the business community along Cochrane Road. He stated that many times, TBI has heard from the corporate users in the Madrone Business Park and the Cochrane Business Ranch that there is a need for additional services in the area during the business day. It is felt that this market can be served by this project. It was also felt that the installation of Madrone Parkway in the Madrone Business Park assessment district was a good thing. TBI believes that it can capitalize on commuters in the area and generate revenue/tax dollars from those using Morgan Hill roads to get through town. The third market is the growing residential population at the north end of Morgan Hill. Therefore, there are three market populations that need to be served and TBI wants the opportunity and flexibility to address each one of these markets.

Mr. Krouskup requested modifications to the PUD uses. He requested that the first item list retail stores. He said that TBI envisions the PUD to be in place for a long period of time. As recommended, he believes that it is confusing and may not address the growing residential population important to a project like this. He concurred with the restaurant designation. He requested the elimination of “health related services” and replaces it with “health related office uses.” He clarified that TBI does not want to construct a medical/dental office building at this location. He noted that the Planning Commission is recommending specialty grocery stores not exceeding 15,000 square feet. He informed the Council that he has had several discussions about this issue over the last several days. He stated that there is an opportunity to have a grocery store on Cochrane Road. He indicated that he has been in close contact with the DiNapoli application being processed on the east side of the Highway. It was agreed that the limitation as a permitted use is acceptable to TBI and DiNapoli as it provides TBI with the flexibility needed to market the project. TBI does not believe that it undermines the intent of a sub regional center to have a major supermarket on the east side of the freeway. He indicated that TBI is proposing this as a conditional use. In talking to John DiNapoli, he indicates that they want to focus on getting a large supermarket on the east side of the highway. However, if this does not come to fruition, he felt that TBI should have the opportunity to try to bring a supermarket to Cochrane Road at some point in time. He clarified that TBI is not talking about a Costco or large supermarket concept, but of a personalized regional/family oriented specialty market, as the site cannot accommodate large supermarkets. TBI believes that a drugstore could be an important component and a great service to the businesses, commute clientele and the residential population. He noted that TBI is proposing wine tasting and arts and crafts galleries (e.g., Michael’s) as permitted uses. Under conditional uses, he requested that the Council approve gasoline service stations with ancillary convenience store and grocery stores exceeding 15,000 square feet.

Council Member Chang disclosed that she spoke with John DiNapoli yesterday who indicated that he is having a problem with a grocery store over 15,000 square feet on the TBI site. She inquired whether Mr. Krouskup and Mr. DiNapoli reached an agreement regarding this concern.

Mr. Krouskup indicated that he spoke with Mr. DiNapoli several times and that as late as this afternoon, they discussed this issue thoroughly. He said that it was his belief that Mr. DiNapoli understood TBI’s proposal. He indicated that Mr. DiNapoli agrees to a grocery store over 15,000 square feet as long as it is a conditional use where the City could review the proposal. He said that TBI would like the center to be anchored in a small way. He said that the project, as laid out, stipulates approximately 72,000-75,000 square feet of retail. TBI would like to anchor this with a use in the neighborhood of 25,000-45,000 square feet. He felt that this is an anchored center and does not consider this as a strip center as he envisions that it will include a pad or two on Cochrane Road with sit down restaurants. Therefore, he considers this to be a small shopping center.

Council Member Carr felt that banks were part of the financial services. In talking about arts & crafts/galleries, he stated that he understood the distinction between a Michael’s and a retail use rather than an art gallery. He felt some of the uses proposed would be better suited for the downtown. He wanted to make sure that what is approved would not be in competition with the downtown.

Mr. Krouskup stated that the intent of the PUD center is to serve the three users he previously addressed. He felt that the uses would be different from the uses found in the downtown. He noted that this would not be a walking center as individuals would be driving to the center. They would be traveling toward a convenience destination and depending on the size of the anchor tenant; a citizen may have a destination. He stated that in large part, the center would be serving the cars already in the traffic pattern, a different purpose from the downtown as individuals going to the downtown have a specific purpose, walking 2-4 destinations and possibly dinner. He indicated that he has heard the comment that the wine tasting might be better suited for the downtown. He stated that wine tasting is not a major component of the PUD. He said that the wine tasting came in as part of a small specialty grocery use of approximately 8,000-10,000 square feet with a wine tasting barn. If this is a use that the City believes would compete with the downtown, he could eliminate this use. Regarding the arts & craft galleries, he indicated that it is proposed to have the “Michael’s” type of retailer; as a result from the fact that 2.5 years ago, Thomas Kinkade indicated that he would like to have a gallery/museum on this site. He felt that this may be a viable option and that it would be good for the City and the project if this use evolves.

Mayor Pro Tempore Sellers said that whether or not the use is specifically listed, he did not believe that it would preclude a Michael’s or a gallery retail store. He did not believe that the use constitutes a separate designation.

Mr. Krouskup stated that the verbiage of arts & crafts galleries and wine tasting comes out of the general commercial zoning district as outlined in the City’s zoning ordinance.

Council Member Tate said that in his meeting with Mr. Krouskup, it was his understanding that the PUD would target customized markets of the size of 30,000-40,000 square feet range. He indicated that Mr. Krouskup has stated that he does not want to go after a supermarket of 50,000+ square feet. He inquired whether there was a better way to specify the intent of having a conditional use of exceeding 15,000 square feet, but less than 50,000 square feet.

Mr. Krouskup stated that he would agree to the stipulation of not recruiting a supermarket of a size greater than 50,000 square feet. He said that the PUD needs to co-exist with the DiNapoli application. He felt that he has expressed his views of what is being sought as part of the PUD and that if this helps to define it better, he would support the intent.

Council Member Chang noted that the City has repeated drugstore uses in Walgreen, Rite Aide, and Longs Drugstores. She inquired what type of drugstore is being proposed and whether it would split the sales taxes versus creating a new sales tax or new business.

Mr. Krouskup responded that he does not have the answer to Council Member Chang’s question at this time. He felt that there was a fairly large population growing that is not being served by a drugstore use and that there will be a need for another drugstore with a pharmacist north of Dunne Avenue. He acknowledged that there were stores such as Target that sell medication and vitamins. He said that he carefully reviewed the grocery store issue. In his meeting with Mr. DiNapoli, they specifically discussed a drugstore. He indicated that Mr. DiNapoli did not have a problem with having a drugstore as a permitted use associated with this project. He did not know if Mr. DiNapoli will have a drugstore in

his development. He said that his project will lend itself to the smaller end of the spectrum but felt that the market dictates whether there is a need for a drugstore on Cochrane Road. He felt that the users that will go on the east side of the freeway versus what will be associated with a 72,000 – 75,000 square foot center being proposed will be different. He would like the market to dictate what will be needed.

No further comments being offered, the public hearing was closed.

Mayor Kennedy stated his support of the proposed changes. He indicated that he met with Mr. Krouskup and felt that the City was losing a lot of its business customers in the Cochrane Road area. He guestimated that there are 5,000-15,000 employees that work in the Morgan Hill Ranch and the Madrone area. He envisions these individuals getting into their cars and driving home. If they have an opportunity to stop at the drugstore or to patronize other services that cater to their needs, this is a market that the City could capture that would help the City's sales tax base and help to provide services to individuals that work at the Morgan Hill Ranch and the Madrone Business Park.

Mayor Pro Tempore Sellers said that in his discussion with TBI and the Cochrane/Highway 101 project, there is a concern that the City has two successful projects. He was encouraged and pleased to hear that discussions took place between the two developers and that they were fruitful. He said that the success of these projects will be the designated uses, complimentary uses and timing. It was his belief that the Cochrane/Highway 101 will have a couple of months lead in terms of its ability to market. Therefore, the City will have an opportunity to see what might be attracted to that site. He felt that both projects would capture those who would bypass the City because their needs are not being met in this area of town. Regarding the drugstore issue, he felt that the market will have a final say on the use. The question will be whether the individuals who reside in the northern part of town will use this drugstore as opposed to going into San Jose or somewhere outside of the City. It was his hope that the build up medical services in the area would support a drugstore as well. He said that he was not pleased to see the prospect of a drugstore at the top of the list but that he supported seeing the use listed under the permitted uses as the market will dictate appropriate uses. He felt that the wine tasting would be ancillary to the drugstore and that an arts & crafts gallery should be defined as a retail use. He did not know if it was important to call these out as specific uses. He stated that this is for clarification purposes and to make a statement that the City is trying to recruit specialized boutique retailers in the downtown. He would support not listing these uses as long as it does not narrow Mr. Krouskup's ability to go out into the market.

Planning Manager Rowe said that in the context in which Mr. Krouskup is proposing the wine tasting as an extension of a retail use, it would be acceptable not to list the use. He confirmed that the two uses under discussion were pulled out of the Highway Commercial zoning district as stand alone uses. This was the kind of tasting room that was envisioned in the zoning district. The same would apply to the arts & crafts use as an opportunity to display and sell items geared toward tourist uses. If the use is more like a Michael's, this use would be covered under the retail uses.

Council Member Carr referred to the Planning Commission minutes, indicating that he could not find the reason why the Commission added the phrase "supportive of the neighboring industrial parks."

Planning Manager Rowe stated that when staff first had discussions with Mr. Krouskup, he was trying to determine whether there would be support, at a staff level, to apply for a general plan amendment. Mr. Krouskup talked about incorporating commercial uses that were supportive of the surrounding business parks. It was staff's belief that this was a good thing because the Morgan Hill Ranch Business Park had a category entitled "non manufacturing business." This category extended all along the south side of Cochrane Road from Sutter Boulevard to Monterey Road. He informed the Council that this category was removed from this PUD approximately five years ago. Therefore, this was an opportunity to reestablish a commercial area that would be able to have office supply stores and financial institutions that would serve businesses. This was the basis for staff's support of the application. It was his belief that the Commission concurred that the site should focus on these types of uses and not compete with the community serving commercial uses that would be located on the east side of Highway 101 as the general plan policy addresses this issue.

City Manager Tewes clarified that this language was not added by the Planning Commission but that it was an initial staff recommendation and that the Planning Commission concurred with the recommended language.

Council Member Tate addressed the wine tasting and the arts & crafts gallery. What he understands from the discussion is that if these are proposed as a specialty or boutique-type of operation, there is concern about the impacts to the downtown. However, if these uses are ancillary retail uses, they would be accepted. He recommended that the Council support Mayor Pro Tempore Sellers' suggestion to state retail stores. If it is to be left as wine tasting and arts & craft galleries, he recommended that they be listed as conditional uses to examine whether the uses are specialty enough to raise concerns.

Council Member Carr would support taking these two uses out and assume that they are listed as retail stores.

Council Member Tate stated that he supported grocery stores exceeding 15,000 but less than 50,000 square feet.

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council unanimously (5-0) **Approved** the Mitigated Negative Declaration.*

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council unanimously (5-0) **Adopted** the General Plan Amendment Resolution No. 5845.*

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council unanimously (5-0) **Waived** the Reading in Full of Zoning Amendment Ordinance No. 1695, New Series, as modified in Exhibit "B."*

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council **Introduced** Ordinance No. 1695, New Series by Title only as follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL***

AMENDING THE ZONING DESIGNATION FROM ML, LIGHT INDUSTRIAL TO PLANNED UNIT DEVELOPMENT FOR A 7.72-ACRE PARCEL LOCATED AT THE NORTHWEST CORNER OF COCHRANE ROAD AND MADRONE PARKWAY IN THE MADRONE BUSINESS PARK (APN 726-33-028) (ZA-04-11: COCHRANE - TBI), incorporating the revised/amended Exhibit "B" by the following roll call vote: AYES: Carr, Chang, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: None.

17. GENERAL PLAN AMENDMENT, GPA-04-03; ZONING AMENDMENT, ZA-04-09: BUTTERFIELD-SOUTH VALLEY DEVELOPERS – Ordinance No. 1696, New Series & Resolution No. 5846

Planning Manager Rowe presented the staff report, a request to amend the land use designation from industrial to multi family, medium density. He informed the Council that staff and the Planning Commission finds that the proposed amendment would be compatible with the surrounding uses. He indicated that the negative declaration includes mitigations for traffic impacts associated with build out of the project. He said that the initial concept, which was the basis of the traffic study, included a mixed use area with approximately 18,000+ square feet of retail use. He stated that staff had concerns about the potential for cut through traffic occurring to bypass the traffic signal at Monterey Road or Butterfield Boulevard. The applicant agreed to come up with a concept that would use the opposite centerline from Cochrane Circle as the main entrance point. The new site layout eliminates the cut through potential and incorporates the open space areas to a more centralized location in the development. He indicated that a driveway will connect through to the Cochrane Village Apartment development which will allow for the elimination of another driveway. This will allow traffic to access the development via the signalized intersection. Based on the revised site layout, two traffic mitigation measures found on page 235 of the agenda packet, TC5 and TC6, can be eliminated from the mitigated Negative Declaration. He noted that a supplemental letter dated September 13, 2004 from Higgins & Associates was distributed to the Council, where they analyzed this new plan. Because of the elimination of the retail use in the mixed use portion, there is a significant reduction in traffic volumes.

Mayor Pro Tempore Sellers stated that he appreciated the change that was made as it is a positive one. He inquired where the natural flow of traffic will be.

Planning Manager Rowe said that there is a circulation aisle that goes around the outer perimeter and a central one that goes through the project. He addressed the traffic patterns for the proposed land use indicating that Butterfield, north of Cochrane will be used. He stated that the housing units will be a combination of for sale and for rent. He said that the new layout decreases the unit count by 2 units.

Council Member Carr said that it was difficult to compare the two plans as one of the plans is a nice colored rendering. He said that in the black and white plan it appears to have more blacktop/concrete and massive parking lots.

Mayor Kennedy opened the public hearing.

Scott Schilling stated that the Council has two site plans before it this evening, indicating that he only meant for the Council to see one. He said that with the original zoning and general plan amendment applications he was required to submit conceptual plans showing possible unit layouts. Both plans before the Council show significant changes from the initial conceptual layout from the ones submitted in order to prepare for a Measure C application submittal. He felt that all of the changes to the layout are improvements from the original layout, including the amount of usable open space located in the central portion of the project. He stated that he is excited about the opportunity to create a housing product that is affordable. He informed the Council that the current goal is to produce a “for sale” product consisting of a multi family condominium and patio townhomes. He noted that the proposed residential product is located by an existing multi family neighborhood. Development will afford integration between the two projects. He indicated that there is a safety issue associated with the Cochrane Village Apartments with their current in and out access because both driveways coming in and out of this project are right in and right out only. He is working with EAH, indicating that they are willing to eliminate the driveway if he can provide an access into both projects. He said that it is proposed to have a nice integration between the two multi-family projects. He will be matching the Cochrane Village Apartments’ craftsman style architecture. Therefore, the entire area will appear to have been master planned.

Mayor Kennedy indicated that he was not fond of the existing craftsman style architecture as it does not have a good appearance.

Mr. Schilling indicated that the project will be reviewed by the Architectural Review Board and that they will make sure that it is a top notched designed project. The ability to master plan the 15 acres will present an upscale feel and give the ability to make a gateway statement at the Cochrane/Monterey intersection. He stated that he is working on the intersection per the City’s recommended guidelines for gateway architecture. The project proposes patio townhome units, extensive landscape buffers and attractive front elevations along the project’s street frontage. He indicated that the site layout is still undergoing changes but that it would be similar to what will be submitted under Measure C in the future. He stated that he has met with the Valley Transportation Authority on the proposed bus stop location and that they have indicated that they would like to see this location fully improved with a bus shelter. He indicated that VTA has agreed to take over the maintenance of the bus stop. VTA has asked that he look into installing a fully improved stop on the north side of Cochrane if the right of way can be obtained.

Mayor Pro Tempore Sellers stated that he appreciates the fact that the garages will not be facing the street frontage. However, it is hard to discern whether a sidewalk is proposed on Cochrane Road.

Mr. Schilling indicated that sidewalks will be installed throughout the entire perimeter of the project and that pathways will tie into the City sidewalks to the exterior of the project.

Mayor Pro Tempore Sellers noted that the frontage on Jarvis will be facing a business park. He expressed concern that residents may complain that industrial buildings are being built across the street.

Mr. Schilling stated that multi family uses are more compatible with light industrial uses, especially if you have a street between the two uses. He said that the business park PUD has significant front setbacks. Therefore, there will be a great separation between the two uses.

Mayor Kennedy indicated that at the Architectural Review Handbook workshop, the Council discussed not using monolithic poured sidewalks but rather to have a landscaped parking strip, moving the sidewalks away from curbs. He felt that this would be important to the project.

Mr. Schilling informed the Council that he proposes to install the sidewalks per City standards which would require a five-foot landscape planter before you get to the sidewalk. This would result in 30 foot setback from the back of sidewalk. You have to have an additional 10 feet in front of the sidewalk to the actual street. This gives you a nice distance from building to the street.

Council Member Chang indicated that when the Council discussed the Architectural Review Handbook, the Council discussed commercial uses, noting that a residential use is proposed. If individuals reside too close the street, she felt that it would be noisy for them.

Mayor Kennedy noted that the buildings are proposed 40-feet from the curb.

Mr. Schilling indicated that staff expressed a similar concern, and therefore, included a condition in the mitigated negative declaration that a sound study be required as part of the subdivision approval process. This would ensure that the interior and exterior noise levels in the park area meet the City's noise standards. He stated that having the park areas more interior to the project will help reduce the noise levels for those residents using the park area. If there is a noise issue, he may be required to use higher rated windows or sound insulation boards or other methods to make sure that the interior noise levels meet requirements. It was his belief that Sobrato High School, Martin Murphy Middle School and Burnett Elementary schools would service this area.

Darryl Fry, business owner, spoke in support of the project. He stated that he owns a mortgage banking firm that moved to Morgan Hill four years ago. He came to town with approximately 55 employees and that he currently has over 100 employees. He said that he is a growing business and that he is concerned about the housing stock in proximity to his business. He felt that it is a wise decision to bring housing into an area where there is a high employment density. He stated that he is having difficulty bringing talented skilled individuals from out of state into Morgan Hill because of the lack and cost of housing stock. He said that with a higher density project, you have lower costs and provide housing units for entry level individuals who come into the community. He felt that an R-3 project is compatible on this corner as this type of housing stock is needed, especially for those working in the area. He felt that the zone change is compatible with the business park. The idea of being able to have a housing project in close proximity to his business is very favorable to him. As a growing business, there is a great need for the lowest cost housing in Morgan Hill. As he drives around, it seems that there are tons of commercial and industrial buildings and space available in Morgan Hill. Therefore, he felt that the conversion of 16 acres into single family residential is an appropriate decision.

Julie Driscoll said that many times companies perform market studies on population and residential densities. They proportion this to how successful their businesses may be in a given area. She was pleased that other businesses are being considered on Cochrane Road and other areas in Morgan Hill. However, she felt that the City needs residences and a denser population to support those businesses; otherwise, they will not be successful on a long term basis.

Mayor Pro Tempore Sellers said that there is a bit of history with this project and that significant controversy surrounded the initial decision to place housing in this location. He noted that Ms. Driscoll stated it was a desire to provide an opportunity to support residential housing for the City's workforce. He said that the residential project that exists today is an island. They do not have services or access to services from this location. Given this fact, the gateway nature of the project and the developments that are occurring on Cochrane Road, he was comfortable with proceeding with the request for approval this evening.

No further comments being offered, the public hearing was closed.

Action: *On a motion by Mayor Pro Tempore Sellers, and seconded by Council Member Carr, the City Council unanimously (5-0) **Approved** the Mitigated Negative Declaration, deleting mitigation measures TC5 and TC6.*

Action: *On a motion by Mayor Pro Tempore Sellers and seconded by Council Member Carr, the City Council unanimously (5-0) **Adopted** the General Plan Amendment Resolution No. 5846.*

Action: *On a motion by Mayor Pro Tempore Sellers and seconded by Council Member Carr, the City Council unanimously (5-0) **Waived** the Reading in Full of Zoning Amendment Ordinance No. 1696, New Series.*

Action: *On a motion by Mayor Pro Tempore Sellers and seconded by Council Member Carr, the City Council **Introduced** Ordinance No. 1696, New Series, by Title only, as follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL AMENDING THE ZONING DESIGNATION FROM PUD, RESEARCH AND DEVELOPMENT/MANUFACTURING TO PUD, R3 MEDIUM DENSITY RESIDENTIAL FOR TWO PARCELS TOTALING 15.78 ACRES IN SIZE, LOCATED AT THE SOUTHEAST CORNER OF COCHRANE ROAD AND MONTEREY ROAD IN THE MORGAN HILL RANCH BUSINESS PARK (APNs 726-25-076 & -077) (ZA-04-09: BUTTERFIELD-SOUTH VALLEY DEVELOPERS) by the following roll call vote: AYES: Carr, Chang, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: None.***

Mayor Kennedy congratulated South Valley Developers for a very well done project as it will fill a need and will correct the problem with a housing development that sits as an island. He felt that this project will make this area a nice residential neighborhood and a part of the community.

18. ZONING AMENDMENT APPLICATION, ZA-04-02: COCHRANE-ASSISTED LIVING CENTER – Ordinance No. 1697, New Series

Planning Manager Rowe presented the staff report, informing the Council that it received a revised design standard matrix dated September 15, 2004 this evening. He stated that the Council will be approving the architectural guidelines and the development standards as required under a PUD zoning district. He informed the Council that the Planning Commission reviewed the request last night and voted 5-0 to recommend Council approval of the zoning application, amending the maximum building height to 35-feet. The Council also received copies of the landscape guidelines which were missing from the material submitted to the Council.

Mayor Kennedy opened the public hearing.

Ricardo de la Cruz, applicant, indicated that he would answer any questions that the Council may have. He informed the Council that he was impressed with the planning staff as they have been helpful throughout the year. He stated that he is continuing to have success with the O'Conner group and that it is his hope to break ground in early 2005 if everything remains on schedule.

No further comments being offered, the public hearing was closed.

Action: *On a motion by Council Member Tate and seconded by Council Member Carr, the City Council unanimously (5-0) **Waived** the Reading in Full of Ordinance No. 1697, New Series*

Action: *On a motion by Council Member Tate and seconded by Council Member Carr, the City Council **Introduced** Ordinance No. 1697, New Series, by Title only as follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A SET OF DEVELOPMENT STANDARDS AND ARCHITECTURAL GUIDELINES FOR THE DE PAUL (FORMERLY SAINT LOUISE) HEALTH CENTER (APNs 728-031-005, 006, 012 & 013)** by the following roll call vote: **AYES:** Carr, Chang, Kennedy, Sellers, Tate; **NOES:** None; **ABSTAIN:** None; **ABSENT:** None.*

City Council Action

OTHER BUSINESS:

19. URBAN LIMIT LINE STUDY STATUS REPORT.

Planning Consultant David Bischoff presented the staff report, indicating that the purpose of this item is two-fold: 1) to update the Council on the status of the Urban Limit Line (ULL) Committee's work to date; and 2) to provide the Council with an opportunity to provide feedback to this committee regarding the direction the project has taken to date. He indicated that staff is looking for Council comments as to whether or not the overall direction that this committee is taking is appropriate. If not, the Committee would like to know this fact. If the Committee is not heading in the right direction, they need to make a

course direction. Should the Committee be in the right course of direction, the Committee will be developing principals and priorities for acquisition of select properties, reviewing the recommendations of the subcommittee for the southeast quadrant, and finalizing their overall recommendations. Once these items have been completed, staff will return to the Council in a workshop setting in December 2004 to fully brief the Council to the draft final recommendation of the Committee, receiving input from the Council before holding a community meeting. He summarized the actions taken by the Committee to date, noting that Mayor Kennedy and Council Member Chang have provided leadership in this effort.

Mr. Bischoff identified the areas to be included in the urban limit line and the greenbelt areas identified to date. He noted that the greenbelt is not proposed to form a boundary around the entire city. Regarding the southeast quadrant, the Committee appointed a five-member subcommittee to specifically come up with a framework for future planning of the area. He informed the Council that the vision created for this area is included as attachment 3 in the Council packet. He summarized that the vision does not propose the area to be a conventional greenbelt but a discrete area where no development would occur. It is being proposed that all lands within this area are to be included within the urban limit line. The transition from the developed areas to the north into San Martin would occur through a transition of urban density, with more density developed properties to the north, and less density developed properties to the south. In this area, there will be significant open space areas and that within this area, a general allocation of land uses would include a 200-acre industrial park. Also, being recommended is approximately 40+ acres around the interchange of Tennant and Highway 101 be reserved for future economic development opportunities. The subcommittee is recommending broad setbacks, trails, and large natural open areas in the open space consisting of approximately 375-500 acres. This would result in approximately 375-500 acres being placed into residential use. Within this residential area, approximately 2,000 residential units could be built. He informed the Council that the subcommittee had an economist working with them on this plan. It was the economist's belief that the plan being proposed is economically feasible and that the increased value that would be generated by incorporation/rezoning the properties could be sufficient to fund many of the public improvements that would need to occur. He stated that the subcommittee believes, as part of their recommendation that any improvements in this area that would serve the community, overall, should be paid by the community. Only those improvements that benefit the southeast quadrant would be paid for by the southeast quadrant property owners.

Mr. Bischoff stated that the subcommittee recommends that a process occur to achieve the vision: 1) an analysis of vacant industrial lands; 2) an area plan be prepared for the southeast quadrant that would identify the exact size of an industrial park and its location, looking at the residential densities and determining where higher/lower densities should be sited; and establishing/developing general policies for development in the area; and 3) develop a specific plan when development is eminent. The specific plan would provide details about development of the area as well as sharing of costs for the infrastructure and phasing of the annexation in development of the area. The subcommittee recommends that the studies for the area plan and the industrial analysis be funded by the City. He indicated that the full committee has not reviewed the work that the southeast quadrant subcommittee concluded approximately a week ago. He stated that staff is looking for comments from the Council on the overall direction being taken to date.

Mayor Kennedy felt that the Committee has made good progress, especially the subcommittee working on the southeast quadrant. It appears that the subcommittee has a plan and a process that should work for everyone. However, the full committee has not had the opportunity to weigh in on the plan itself. He noted that the urban limit line is drawn around approximately 80% of the city. The committee has established principals and policy statements on how this can be implemented on a map. He felt that the process is working and that the Committee is coming close to the end.

Council Member Chang referred to principal 19 that address low intensity public facilities. She inquired how one would define low intensity public facilities.

Mr. Bischoff indicated that at the meeting of the ULL Committee held on Monday evening, the Committee combined the two items into one. He felt that the Committee was addressing having such things as parks but that he did not believe that they would support an aquatics center. In terms of a low intensity public facility, he felt that the intent of a passive park was having ball fields without bleachers, lighting or restroom facilities.

Mayor Kennedy opened the floor to public comment.

Gordon Jacoby stated that Mr. Bischoff indicated that as part of the ongoing work, a study be conducted on vacant industrial land. He distributed a study he prepared on vacant industrial land and noted that the general plan, as part of the greenbelt study, called for a look at a business park on the east side of Tennant Avenue. He indicated that the committee, as well as the subcommittee, has looked at this but felt that it stopped short of making any decisions on an exact location for an industrial park and what it might look like. He said that the committee felt that there is an adequate amount of land within the City for business development because there were approximately 360 acres of industrially zoned land. While technically correct, he did not believe that this was correct from a market stand point. He noted that the table he presented shows approximately 76 industrial parcels. Of these parcels, most are in the Cochrane area. He said that there would have been approximately 160 acres of high quality vacant land south of the CDF fire station with good access. He stated that the remaining 200 acres are scattered in a way that makes them unattractive. In some cases, they are spread on either side of the railroad, between Dunne and Tennant Avenues. He said that he did not know that there were approximately 50-60 acres of industrially zoned land south of the CDF fire station between Monterey Road and the railroad tracks. He indicated that the reason that these areas remain vacant is due to the fact that the market is by passing them. They have not been viewed as attractive parcels. He felt that the City has 160 acres of industrial zoned land. He said that between 1997 and 2001, the City used 240 acres of industrially zoned land. He felt that the City is being underserved and that if the market picks up, the City will be out of prime industrial locations. He stated that the general plan identified some sites for industrial development; one on the east side of the City around Main Avenue, and one south of Tennant Avenue. He felt that these sites were unworkable, particularly the one behind Tennant Avenue. He said that there are approximately 28 parcels, half of which have homes on them with one of the 1-1.5 acre homes selling for \$800,000. He did not believe that anyone would want to buy land in this area because the price is higher than what industrial land is selling for.

Mayor Kennedy said that statements have been made that the City has over 70 million square feet of vacant industrial building space available in Santa Clara County and inquired why there is a need for more.

Mr. Jacoby indicated that last year alone, 15 million square feet was absorbed in new leases. While this is a large number, it is low compared to any other year. Therefore, it was his belief that vacant land is low. He agreed that there is an ample supply of industrial land. However, he states that you need to understand that the dynamics of Silicon Valley can absorb the vacant industrial building space in a 3-5 year period. He also felt that the City needs to think about what the competition is doing. He stated that San Jose has 9 million square feet of vacant industrial buildings at this time. However, they are trying to get ahead of the curve as it takes 5-7 years to build a business park. You have to look out quite a ways because of regulatory requirements and accumulate land in order to install the infrastructure. He noted that Coyote Valley is installing an interchange. Gilroy has adopted a 600-acre industrial park and is in a position to move toward the next cycle. He felt that there was a need to move forward for the planning of a business park and that it will work well if done as part of the area plan; recognizing that getting to the area plan is a 3-year process. Adding a specific plan, subdivision work and financing of the improvements would result in up to a decade away from having a new business park. He recommended that the Council give direction that this needs to be accelerated as part of the area plan in order to recognize the competition from the north and the south of Morgan Hill. He further suggested that the Council give a sense of where the business park should be as the southeast quadrant is already subdivided and that individuals will start to make decision over the next 2-3 years. He said that once a house is built on a lot, the economics goes crazy and so will future opposition.

Julia Driscoll addressed the southeast quadrant, indicating that many parcels in this area are prime parcels. These parcels have easy access to the freeway and are adjacent to the Institute of Mathematics and the aquatics center is nearby. These parcels are considered to be easily developable because they are flat land. She noted that the utility lines are not located far away. She finds it objectionable that property owners should be bearing some of the costs for whatever is developed. She felt that land is a prime commodity in the supply and demand principal and that the property owners should be in the driver's seat. She did not believe that the property owners should be incurring costs for development. She felt that development should come to property owners and that the property owners should be compensated fairly, adequately and handsomely for what the properties are worth.

Art Fuliaffico, member of the full ULL committee, felt that there was one fatal flaw in the idea of waiting for a specific plan; that is Measure C. When the area is ready for development, it will be imminent that a specific plan be derived. He said that it will be 20-30 years before development is allowed to occur because Measure C prohibits this area from being annexed into the City until there is 5% or less supply of available housing. He noted that commercial and industrial park development is not prohibited by Measure P from being annexed into the City. He said that property owners are overwhelmed with giving up and making concessions for possible commercial/industrial development and waiting for housing development 20-30 years down the road. He noted that it is being requested that a vast amount of open space be given as a concession. He said that most property owners do not understand why they should be giving up half of their lands or 500 acres of projected open space for

something that will not happen for 20-30 years. He felt that what you will see is 10 acre ranchettes developing versus waiting 20-30 years to develop lands.

Joe Mueller stated that this was an opportunity for Morgan Hill, landowners, and those individuals interested in development to work together and plan the largest open area in the City of Morgan Hill. He felt that the City has one shot to plan open space right and develop something that will be an asset/benefit to everyone. This is why the subcommittee and full committee have been looking at going through an area plan and then a specific plan. He felt that the City would lose the opportunity to conduct an integrated, well designed section of the community if allowed to be piecemealed over time. He felt that this will be a huge asset for Morgan Hill when it comes into the community. Being discussed is distributing open space throughout the community so that it maintains what Morgan Hill should feel like. He said that the industrial concerns raised by Mr. Jacoby and the timing are more complex than alluded. He stated that the nature of work is changing and that the nature of business parks in the future may not be that of multiple hundreds of acre. It may be that you need 100 acres integrated in one area. You may need 40-60 acres integrated around commercial and residential development. He felt that the new generation of workers are knowledgeable workers and not factory workers. The study being recommended is more complex than just looking at an inventory of land. The study will be looking at the nature of work as we move forward in this timeframe and how Morgan Hill will have to compete with what will take place in the future. He stated that the industrial land to the north will be going through a tremendous change as it evolves. He felt that it was critical to start the study and move forward as rapidly as possible because the City needs to evaluate some of the less desirable areas. The City needs to be clear in its vision of what the industrial land is to be, as well as its location. He noted that the newest industrial building being built and occupied is located next to one of the areas Mr. Jacoby suggested is not desirable, south of Tennant Avenue.

Richard Place indicated that he was representing some of the land owners who have held a few meetings to discuss the concept of the industrial space. He stated that he sees the value of creating a large parcel for industrial development because it creates an economic situation where a larger company may seek a piece of land that has not been previously developed. He said that undeveloped land would be less expensive to purchase, design and develop. He did not believe that the City has a large parcel of land available in its inventory. He stated that he likes the idea of long term planning and conceptualization. However, there is a situation in the area where there are a number of landowners, some with ethnic backgrounds who have a certain mistrust of government. He felt that it was important to reassure these landowners in the process. This can be done in written form, commitment and contracts with the citizens of Morgan Hill. He did not believe that the process is impossible. He inquired whether landowners could be brought into Measure C, economically in 2020. He felt that if the citizens of Morgan Hill want to proceed, they need to make a commitment. He felt that this would require an analysis and understanding on the part of property owners in this area.

No further comments were offered.

Council Member Chang inquired as to the cost per acre of industrial land to the north versus the cost in Morgan Hill.

Mr. Jacoby indicated that in the height of industrial development, the cost of developed land was \$11 per foot in Morgan Hill in 2000. He stated that the smaller buildings being built in Morgan Hill Ranch are receiving a greater value than the \$11 per foot. Developed industrial areas in Sunnyvale or Santa Clara at that time could have gone as high as \$18 per foot for comparable uses, in some cases. He said that Morgan Hill has been successful in competing because it could sell for \$3-\$4 below for comparable buildings to the north. In south San Jose, the cost was \$2 below. He indicated that businesses were able to relocate to Morgan Hill from the north because they could purchase a brand new building for a cheaper price. He felt that the trend to being able to purchase a brand new building at a lower price continues in Morgan Hill.

Mayor Pro Tempore Sellers stated that he appreciated the fact that staff is checking in with the Council. He said that it was helpful to hear the process that is being undertaken as the majority of the Council does not sit on the committee. Overall, he stated that he was comfortable with the direction the committee is heading. He appreciated the comments expressed by individuals this evening. He said that the solution to the concerns of Measure C is good planning overall. He recommended that the concepts be incorporated and that answers to the questions relating to Measure C be provided. He felt that the comments regarding industrial lands are speculative at this time. He agreed that there are differences in looking at how industrial lands are being absorbed and where the City wants to go with industrial development. He felt that the City needs to plan for the next generation in terms of industrial planning. He supported continuing to have valuable land preserved for open space. He said that it was prohibitively expensive to preserve land that is currently in agricultural use. If the City is going to incorporate these areas, the City needs to look at retaining open space and parks; paying for these amenities as a community in such a way that maximizes the value to the community. He stated that he wants to know the costs of the plans in order to determine whether they were ones that the City should pay for. If so, the City needs to determine how the studies will be paid for.

Council Member Carr stated that he was concerned about the costs. He said that each additional step will cost the City something and recommended that the Council take a look at the costs. He noted that staff discussed the infrastructure improvements at the southeast quadrant and that if they are regional improvements, they need to be paid for regionally. If they are local improvements, these should be paid locally. He felt that the City needs to better define regional improvements and how they will be paid for. It was his hope that when the study looks at vacant industrial lands that the study includes opportunity sites as well as the sites that are no longer good sites for industrial. He felt that there may be great residential opportunity sites that are currently zoned industrial that the City can be looking at.

Mayor Kennedy stated that the planning for the southeast quadrant is not unlike the planning that is being done for Coyote Valley. This will be a long range master plan. He felt that the City may want to consider triggers for this area. He said that at the last meeting of the ULL committee, the committee spent a lot of time talking about greenbelts/green spaces to be preserved. He noted the City has been building up its funds for open space acquisition and that this fund is close to \$900,000. He indicated that one of the issues that the committee will be wrestling with is how to prioritize the acquisition of open space/open space easements. He noted that there are spaces on El Toro that are designated as greenbelt that are privately owned. This is a landmark in the community that it is a high priority for the community. He inquired whether the City should earmark money for the preservation of El Toro or

Mount Hill, the east/west foothills. He indicated that these are issues that the committee is wrestling with and that it will be looking at how to prioritize the expenditures of funds; leveraging the funds with the Open Space Authority or other grant organizations.

Action: *No action taken.*

FUTURE COUNCIL-INITIATED AGENDA ITEMS

No items were identified.

RECONVENE TO CLOSED SESSION

Mayor/Chairman Kennedy announced that the Council/Agency Board would reconvene to closed session to conclude its discussion of the above listed closed session items.

Mayor/Chairman Kennedy opened the closed session items to public comment. No comments were offered

Mayor/Chairman Kennedy adjourned the meeting to Closed Session at 9:43 p.m.

RECONVENE

Mayor/Chairman Kennedy reconvened the meeting at 10:14 p.m.

CLOSED SESSION ANNOUNCEMENT

Mayor/Chairman Kennedy announced that no reportable action was taken in closed session.

ADJOURNMENT

There being no further business, Mayor/Chairman Kennedy adjourned the meeting at 10:15 p.m.

MINUTES RECORDED AND PREPARED BY:

IRMA TORREZ, CITY CLERK/AGENCY SECRETARY

**CITY OF MORGAN HILL
JOINT SPECIAL AND REGULAR REDEVELOPMENT
AND SPECIAL CITY COUNCIL MEETING
MINUTES – SEPTEMBER 22, 2004**

CALL TO ORDER

Chairman/Mayor Kennedy called the special meeting to order at 5:45 p.m.

ROLL CALL ATTENDANCE

Present: Agency/Council Members Sellers, Tate and Chairperson/Mayor Kennedy
Late: Agency/Council Members Carr (arrived at 6:04 p.m.) and Chang (arrived at 6:55 p.m.)

DECLARATION OF POSTING OF AGENDA

Agency Secretary/City Clerk Torrez certified that the meeting's agenda was duly noticed and posted in accordance with Government Code 54954.2.

City Council Action

1. CONDUCT INTERVIEW AND APPOINT TO FILL A VACANCY ON THE MOBILE HOME RENT COMMISSION.

The Council interviewed Eric Gould, applicant, interested in serving on the Mobile Home Rent Commission.

Mayor Kennedy informed Mr. Gould that the Council would consider his application to serve on the Mobile Home Rent Commission and thanked him for his interest in wishing to serve the City and the community on this Commission.

Council/Agency Member Carr entered and took his seat on the dias.

Action: *No action taken.*

Redevelopment Agency and City Council Action

CLOSED SESSIONS:

Mayor/Chairman Kennedy announced the below listed closed session items.

- | | |
|--|---|
| 1. | |
| <u>CONFERENCE WITH LEGAL COUNSEL - ANTICIPATED LITIGATION</u> | |
| Authority: | Government Code Sections 54956.9(b) & (c) |
| Number of Potential Cases: | 2 |

2.

PUBLIC EMPLOYEE PERFORMANCE EVALUATION

Authority	Government Code 54957
Public Employee Performance Evaluation:	City Manager
Attendees:	City Council, City Manager

3.

PUBLIC EMPLOYEE PERFORMANCE EVALUATION

Authority	Government Code 54957
Public Employee Performance Evaluation:	City Attorney
Attendees:	City Council, City Attorney

4.

CONFERENCE WITH LEGAL COUNSEL - EXISTING LITIGATION:

Authority:	Pursuant to Government Code 54956.9(a)
Case Name:	City of Morgan Hill v. Howard Vierra
Case Number:	Santa Clara County Superior Court, Case No. 1-04-CV-026723

Council/Agency Member Chang was not in attendance during closed sessions.

OPPORTUNITY FOR PUBLIC COMMENT

Chairman/Mayor Kennedy opened the Closed Session items to public comment. No comments were offered.

ADJOURN TO CLOSED SESSION

Chairman/Mayor Kennedy adjourned the meeting to Closed Session at 6:05 p.m.

RECONVENE

Agency/Council Member Chang entered and was seated.

Chairman/Mayor Kennedy reconvened the meeting at 7:10 p.m.

CLOSED SESSION ANNOUNCEMENT

Chairman/Mayor Kennedy indicated that the Redevelopment Agency Board/City Council continued the closed sessions to the conclusion of the regular meeting agenda.

Acting Agency Counsel/City Attorney McClure announced that there was nothing to report out of closed session at this time.

SILENT INVOCATION

PLEDGE OF ALLEGIANCE

RECOGNITIONS

On behalf of the City of Morgan Hill, Mayor Kennedy presented a Certificate of Recognition to Ms. Loritta Johnson, in honor of her receiving the Santa Clara County Office of Education Teacher Recognition Award.

COMMENDATION

Mayor Kennedy presented a Certificate of Commendation to Police Officer David Ray for his act of heroism in pursuit of a suspect attempting to cash a forged check with false identification. The suspect fled the scene and unsuccessfully attempted to carjack a passing vehicle. While risking his own safety, Officer Ray pursued the suspect and successfully/heroically gained control of the suspect while chasing him across several lanes of heavy traffic. Officer Ray averted a potentially dangerous situation involving several citizens, theft of property, and injury to himself and others, by handling this event in an extremely professional manner.

Interim Chief of Police Cumming informed the Council that the potential carjack victim knows Santa Clara County Board of Supervisor Pete McHugh and told him of Officer Ray's act of heroism. Supervisor Pete McHugh also wrote up a commendation for Officer Ray to which he read into the record.

CITY COUNCIL REPORT

Council Member Chang announced that she would be on a 4-6 week medical leave of absence and excused herself from the remainder of the meeting.

PUBLIC COMMENT

Chairman/Mayor Kennedy opened the floor to public comment for items not appearing on this evening's agenda. No comments were offered.

Redevelopment Agency Action

CONSENT CALENDAR:

Action: *On a motion by Agency Member Tate and seconded by Vice-chairman Sellers, the Agency Board, on a 4-0 vote with Agency Member Chang absent, **Approved** Consent Calendar Item 2 as follows:*

2. **AUGUST 2004 REDEVELOPMENT AGENCY FINANCE & INVESTMENT REPORT**
 Action: **Accepted** and **Filed** Report.

City Council Action

CONSENT CALENDAR:

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council, on a 4-0 vote with Council Member Chang absent, **Approved** Consent Calendar Items 3-7, as follows:*

3. **AUGUST 2004 FINANCE & INVESTMENT REPORT**

Action: ***Accepted** and **Filed** Report.*

4. **FINAL MAP APPROVAL FOR MORGAN STATION (TRACT 9585)**

Action: *1) **Approved** the Final Map, Including the Abandonment of an Excess Portion of East Central Avenue; 2) **Approved** the Subdivision Agreement and Improvement Plans; 3) **Authorized** the City Manager to Sign the Subdivision Improvement Agreement on Behalf of the City; and 4) **Authorized** the Recordation of the Map and the Subdivision Improvement Agreement Following Recordation of the Development Improvement Agreement.*

5. **INDOOR RECREATION CENTER – APPROVE CONSULTANT AGREEMENT FOR PHASE I CONSTRUCTION MANAGEMENT SERVICES**

Action: ***Authorized** the City Manager to Execute a Consultant Agreement with Nova Partners, Inc. for a Total Fee not to exceed \$114,800, Subject to City Attorney Review and Approval.*

6. **REJECTION OF BIDS FOR BOYS RANCH RESERVOIR #3**

Action: ***Rejected** the Bids Received on September 8, 2004 for the Construction of the Boy's Ranch Reservoir #3 and **Authorized** Staff to Re-bid the Project.*

7. **JOINT SPECIAL CITY COUNCIL, SPECIAL PLANNING COMMISSION, AND SPECIAL ARCHITECTURAL REVIEW BOARD MEETING MINUTES OF SEPTEMBER 8, 2004**

Action: ***Approved** the Minutes as Written.*

Redevelopment Agency and City Council Action

CONSENT CALENDAR:

Action: *On a motion by Agency/Council Member Tate and seconded by Vice-chair/Mayor Pro Tempore Sellers, the Agency Board/City Council, on a 4-0 vote with Agency/Council Member Chang absent, **Approved** Consent Calendar Items 8 and 9 as follows:*

8. **CARRYOVER OF ENCUMBRANCES FROM FISCAL YEAR 2003-2004**

Action: ***Received** and **Filed** Report.*

9. **FINAL FISCAL YEAR 2003-2004 BUDGET ADJUSTMENTS**

Action: *Approved the Proposed Final Budget Adjustments for Fiscal Year 2003-2004.*

Executive Director/City Manager Tewes informed the Agency/Council that it adopted a policy whereby public hearings are considered on or after 7:30 p.m. He therefore recommended that the Council consider agenda item 12 at this time.

Redevelopment Agency Action

OTHER BUSINESS:

12. **EXTENSION OF EXCLUSIVE RIGHT TO NEGOTIATE AGREEMENT (ERN) WITH EL TORO BREWING.**

Director of Business Assistance and Housing Services Toy presented the staff report, informing the Council that the developer is requesting that the Agency Board extend the initial extension of October 12 to November 30, 2004 to allow him additional time to secure financing. He indicated that the revised agreement provides for a 60-day extension if the lender needs additional time to approve the El Toro Brewing loan. He said that closing on the property is approximately 60-90 days longer than anticipated. However, staff believes that El Toro has made good faith efforts to have ARB approval and that they are close to securing their financing. He indicated that the Economic Development Committee members (Agency/Council Members Carr and Tate) are recommending approval of the extension.

Vice-chairman Sellers stated that he was please to see that closing of escrow and the approval of the construction loan would occur simultaneous. He did not know what would happen should the property close escrow and the construction loan falls through.

Mr. Toy said that it would make sense to have the bank fund the loan at the same time that escrow closes as this would ensure that the developer would have their construction financing in place.

Vice-chairman Sellers recommended that the terms of the agreement reflect that the bank loan and close of escrow should coincide with each other.

Chairman Kennedy opened the floor to public comment. No comments were offered.

Action: *On a motion by Agency Member Carr and seconded by Agency Member Tate, the Agency Board, on a 4-0 vote with Agency Member Chang absent, **Authorized** the Executive Director to Prepare, Negotiate, and Execute an Amendment to the ERN with El Toro Brewing to Extend the ERN Deadline to November 30, 2004, with Provisions to Allow for a 60-Day Extension Subject to Specific Conditions as Detailed in the Revised Schedule of Performance.*

City Council Action

PUBLIC HEARINGS:

10. DEVELOPMENT AGREEMENT FOR DAN GAMEL, INC. – *Ordinance No. 1698, New Series*

Director of Business Assistance and Housing Services Toy presented the staff report, indicating that the development agreement memorializes the significant benefits to the City and the developer. He highlighted the key business terms of the development agreement. He indicated that a Council subcommittee, consisting of Mayor Kennedy and Council Member Tate, have worked with staff to craft and negotiate the development agreement and are recommending its approval. He informed the Council that Jim Patterson with Dan Gamel RV was in attendance to answer any questions the Council may have.

Council Member Carr requested that staff explain how the \$20.7 million base amount was calculated. He inquired as to the amount of sales taxes that were generated last fiscal year.

Mr. Toy said that in the previous agreement, the City established a base line amount and that staff carried that amount into this agreement. In the last year of the ten year agreement (Fiscal Year 02-03), it established the base line of approximately \$200,000. Staff applied a CPI to it and came up with a new baseline figure of \$20.7 million and that staff carried over the concept of increasing it by the CPI each year. He clarified that Dan Gamel's RV exceeded \$20 million in sales in Fiscal Year 2002-03. He informed the Council that sales tax information is confidential but stated that Dan Gamel exceeded the baseline amount and that they received a rebate.

Council Member Carr noted that the baseline of the agreement did not start at the current level of sales but at the ending point of the last agreement, plus CPI.

Mayor Kennedy opened the public hearing. No comments being offered, the public hearing was closed.

Council Member Carr inquired whether the Council Economic Development subcommittee felt that the City was challenging Dan Gamel to meet a certain threshold or was the City falling back to where it was in the last agreement.

Council Member Tate felt that henceforward, the City would be challenging Dan Gamel to meet the phasing or the other challenging thresholds. He stated that he was not sure whether the subcommittee was challenging Dan Gamel on the base line. The Subcommittee agreed to keep the baseline going from where the agreement terminated.

Mayor Kennedy stated that the subcommittee used the baseline as a starting point. He indicated that this was not an easy process and that it was a difficult journey to get to this point. The subcommittee wanted to ensure that the City did not lose a valuable business in the community. Therefore, there was a lot of give and take in the negotiation of the agreement.

City Manager Tewes stated that the agreement that was entered into 12 years ago identified a threshold and that it was for a straight 50% sales tax sharing of every dollar. He said that this agreement was structured with an attempt to give an incentive to Dan Gamel to expand in operations and increase sales. Therefore, the schedule that is shown in the agreement is not 50% of the lower levels. The agreement only achieves more than 50% at high levels of sale.

Mayor Kennedy said that the good news is that Dan Gamel's RV has been doing quite well and that their sales have been excellent. He said that the potential for growth is good.

Mayor Pro Tempore Sellers noted that the City is looking at spending money to move the house associated with item 11 to a place where activity will be taking place soon. He inquired whether the City would be incurring additional costs in moving the house again in the near future.

Mr. Toy stated that staff proposes to move the house to its permanent location on the site which would be close to the existing pump house of the soccer complex, its permanent location as part of future development.

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council, on a 4-0 vote with Council Member Chang absent, **Waived** the reading in full of Ordinance No. 1698, New Series.*

Action: *On a motion by Council Member Tate and seconded by Mayor Pro Tempore Sellers, the City Council **Introduced** Ordinance No. 1698, New Series, by Title Only as follows: **AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING A DEVELOPMENT AGREEMENT WITH DAN GAMEL, INC. FOR THE EXPANSION OF DAN GAMEL'S MORGAN HILL RECREATIONAL VEHICLE (RV) CENTER**, by the following roll call vote: AYES: Carr, Kennedy, Sellers, Tate; NOES: None; ABSTAIN: None; ABSENT: Chang.*

Redevelopment Agency Action

OTHER BUSINESS:

11. AWARD CONTRACT TO ABCO CONSTRUCTION TO MOVE THE HISTORIC LA MALFA HOUSE.

Director of Business Assistance and Housing Services Toy presented the staff report, indicating that the house was deemed to be a historical building by a third party, a historical consultant retained by the City. He stated that staff intends to store the house on the soccer complex site for future development as a sports complex and move it to its permanent location.

Chairman Kennedy indicated that there are a few other historical significant items on the site such as tractors and cars used for hauling crates of prunes and apricots from the dehydrator part of the facility. These are unique agricultural handling equipment that are old in nature that will be saved.

Mr. Toy informed the Agency Board that the funds to move the house come will from the Redevelopment Agency Fund (80% monies).

Vice-chairman Sellers felt that it would be important to know the historical significance of the house, who resided in the house and other attributes for making the structure significant.

Mr. Toy said that staff has the report prepared for the house and stated that the house is considered to be of historical significance because the La Malfa family lived in the house and were influential in this area when it came to vintners and agriculture type industry. He indicated that the house was built in 1906. Therefore, the combination of the age of the home as well as the historical significance of the family and the winery lent itself to the historic fabric of Morgan Hill. Thus, the reason the house was deemed significant.

Chairman Kennedy said that the house has a lot of architectural features that are in good shape and unique. He was pleased that the house was being saved.

Mayor Kennedy opened the floor to public comment. No comments were offered.

Action: *On a motion by Agency Member Tate and seconded by Vice-chairman Sellers, the Agency Board, on a 4-0 vote with Agency Member Chang absent, **Awarded** \$30,000 Construction Contract to ABCO Construction for the La Malfa House Move, subject to Review and Approval by Agency Counsel*

Action: *On a motion by Agency Member Tate and seconded by Vice-chairman Sellers, the Agency Board, on a 4-04 vote with Agency Member Chang absent, **Authorized** the Expenditure of Contingency Funds Not to Exceed \$6,000.*

City Council Action

OTHER BUSINESS:

13. WATER RATES

Finance Director Dilles presented the staff report, indicating that previously, the City Council adopted a series of water rate increases and perchlorate surcharge increases over the next several years. At the time the Council adopted these increases, the Finance Director was required to return to the Council by the September prior to each January increase and report on the necessity of the upcoming increases. He stated that the City has a scheduled 2% water rate increase in January 2005 along with a scheduled 5% surcharge increase. He indicated that the proposed water rates assume some recovery costs from Olin Corporation. He informed the Council that it will be necessary to increase the surcharge from 5% to 10% and to increase water rates another 2% in January 2005 in order to stay close to the funding that is needed to pay for projected costs.

City Manager Tewes informed the Council that the Tennant Avenue well is not yet in operation as the City is awaiting license approval from the California State Department of Health Services.

Council Member Tate noted that the City has perchlorate costs in the amount of \$3.5 million and has a recovery from Olin Corporation of \$1.3 million. This results in a \$2.2 million deficit that the analysis shows the rate payers will have to pay in surcharges. He stated that the analysis does not show that the City will attempt to recover this cost from Olin Corporation.

City Manager Tewes said that it will be the City's intention to seek reimbursement from Olin Corporation. He said that the City has received some reimbursements from Olin Corporation and that it is included in the actuals for 2003-04. He said that the City has an identifiable cost for which the City will be making a claim for the second emergency well. He stated that the technical and operating costs are not likely to be recovered until such time as there is subsequent legal action and that staff did not know when to insert these costs. He stated that it was the Council's direction that staff seeks recovery of all perchlorate related costs and that the rate payers should not bare the burden of the contamination of the groundwater by Olin Corporation.

Council Member Carr said that if and when the City receives additional money from Olin Corporation or if in fact the bill sponsored by Congressman Pombo passes, these dollars will come to the City. These monies will allow the City to balance against the perchlorate surcharge that the rate payers are paying.

Finance Director Dilles stated that the resolution before the Council requires that this money be credited back to the rate payers and can only be used for perchlorate purposes.

City Manager Tewes stated that Congressman Pombo's bill would not provide any direct benefit to Morgan Hill's rate payers but would provide for future remediation of the groundwater. He clarified that the Bill would not provide for repayment of past costs.

Finance Director Dilles said that the reason the City will be \$300,000 short of its target in June 2007 is because there is an assumption that the Santa Clara Valley Water District will continue to substantially increase the City's pump tax. He stated that he and other staff members are working with the Water District on their Retailers Committee trying to understand the components of their costs and provide input. He said that the Water District is proposing significant increases to both north and south county that they believe are necessary to operate the Water District. Without these projected increases, the City would not be seeing this particular shortfall.

Mayor Kennedy inquired whether the City has noticed any reduction in water usage due to conservation efforts or the cooler weather.

City Manager Tewes said that the City's daily peak was shorter this year than it was last year. He said that the peak versus the City's capacity determines whether or not it needs to engage in water emergency actions. Because of the cooler summer, the peak daily use has been less this year than in the prior year. However, for total water consumption, the City's water system is trending toward an increase in total water consumption this year as compared to last year. He clarified that the peak is lower but that the total consumption is up.

Mayor Pro Tempore Sellers expressed concern with the 100% water rate increase in four years. He said that if the City does not increase its perchlorate surcharges and Olin Corporation does not reimburse the City, the City would end up with a funding balance of zero within three years.

Council Member Carr inquired whether the capital cost associated with recycled tertiary water was too great for Morgan Hill to try to begin this conversation as a way of reducing water usage.

City Manager Tewes indicated that the City's general plan requires that the City consider the use of recycled tertiary water. He said that as the South County Regional Wastewater Authority (SCRWA) considers its plans for expansion and the disposal of treated wastewater, there is the potential for pumping it back up hill which added to the costs. He said that there has to be enough usage of the tertiary treated water in parks and large users to make it viable.

Director of Public Works Ashcraft informed the Council that SCRWA and the Water District's work plan this year includes a report on the long term master plan for recycled water use. He indicated that Gilroy has been receiving treated wastewater for various usages (e.g., golf courses and parks) for some years. He said that this plan projects some costs that may be cost effective for Morgan Hill to receive some recycled wastewater. One instance would be to pump recycled wastewater for 10 miles. However, the cost of this would be exorbitant and that it would be some time before this can become cost effective. Another possibility would be to construct a separate stand alone tertiary treated scalping plant in Morgan Hill using this water for irrigation. However, this alternative would need several dedicated customers who would use the tertiary water to irrigate. He indicated that the City does not have these customers yet. He stated that the City's parks are diversely located throughout the City and that it would be difficult to plumb these into one irrigation system. He stated that there is a golf course in the south and eastern part of town that could benefit from the recycled water and that this is mentioned in the plan. He indicated that the plan would be coming before SCRWA within the next six months and that following SCRWA's review; the two councils will get to spend more time on this issue.

Mayor Kennedy inquired whether it would make sense for the City to conduct a local study of the scalping plant in conjunction with the Math Institute golf course as the user of recycled water (e.g., feasibility study).

Director of Public Works Ashcraft indicated that a feasibility study is being undertaken by the Water District with a consultant in a macro review. When the study comes before the Council, the City might decide to branch out further and look into this area in more depth. He felt that it made sense to wait for the conclusion of the SCRWA study in six months. At that time, the City might get into more detail if the Council felt that it would be cost effective. He indicated that the study includes looking at a scalping study in Morgan Hill. It was his belief that the study includes a possible user of recycled water located near the eastern side of Morgan Hill.

Mayor Kennedy requested that staff provide the Council with an update on the study sometime in the future.

Mayor Kennedy opened the floor to public comment. No comments were offered.

Action: *By consensus, the City Council **Accepted** and **Filed** the Report.*

FUTURE COUNCIL-INITIATED AGENDA ITEMS

No items were identified.

RECONVENE TO CLOSED SESSION

Chairman/Mayor Kennedy indicated that the Council would reconvene to Closed Session to discuss the items as listed on the agenda.

Acting Agency Counsel/City Attorney McClure indicated that anticipated litigation, personal matters relating to the City Attorney, and the performance evaluation of the City Manager would be discussed in closed session.

Chairman/Mayor Kennedy reconvened the closed session at 8:02 p.m.

RECONVENE

Chairman/Mayor Kennedy reconvened the meeting at 8:59 p.m.

CLOSED SESSION ANNOUNCEMENT

Acting City Attorney/Agency Counsel McClure announced that under Closed Session Item 1, Anticipated Litigation, it was reported that the Council approved a settlement of a claim made by the City Attorney against the City of Morgan Hill. The City Council authorized the City Manager to execute the settlement agreement and its release, once it has been approved by City Attorney Helene Leichter. No other reportable actions were taken in closed session. Council/Agency Member Chang was not in present during closed session discussions.

ADJOURNMENT

There being no further business, Chairman/Mayor Kennedy adjourned the meeting at 9:00 p.m.

MINUTES RECORDED AND PREPARED BY:

IRMA TORREZ, AGENCY SECRETARY/CITY CLERK



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Development Agreement DA-04-03: DeWitt-Latala

RECOMMENDED ACTION(S):

1. Open/Close Public Hearing
2. Waive the First and Second reading of Development Agreement Ordinance
3. Introduce Development Agreement Ordinance (roll call vote)

EXECUTIVE SUMMARY: A request to approve a development agreement for a four-unit project located on a 1.45-acre site on the west side of DeWitt Avenue approximately 500 feet south of Oak Park Drive. The zoning for the site is R1-12,000 RPD. In the 2003 Micro Measure P competition, the applicant received three allocations for FY 2005-2006. The complete project will be four units; the applicant will receive credit for an existing unit. The applicant has submitted his tentative parcel map, which is being processed by City staff.

The applicant is requesting approval of the project development agreement. Project development agreements are required as a formal contract between the developer and the City. The development agreement formalizes the commitments made during the Measure P process and establishes the development schedule for the project. The project specific commitments are identified in Paragraph 14 of the development agreement, and the development schedule is contained in Exhibit B.

The Planning Commission reviewed the application at their September 14 meeting, at which time the Commission voted 6-0 to recommend approval of the development agreement as prepared. The Planning Commission staff report and draft minutes are attached for Council's reference.

FISCAL IMPACT: None. Filing fees were paid to the City to cover processing of this application.

Agenda Item # 18

Prepared By:

Associate Planner

Approved By:

Planning Manager

Submitted By:

City Manager

ORDINANCE NO.

**AN ORDINANCE OF THE CITY COUNCIL OF THE CITY
OF MORGAN HILL APPROVING DEVELOPMENT
AGREEMENT, DA 04-03: DEWITT-LATALA FOR
APPLICATION MMP 03-06: DEWITT-LATALA. (APN 773-
08-012)**

**THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY
ORDAINS AS FOLLOWS:**

SECTION 1. The City Council has adopted Resolution No. 4028 establishing a procedure for processing Development Agreements for projects receiving allotments through the Residential Development Control System, Title 18, Chapter 18.78 of the Municipal Code.

SECTION 2. The California Government Code Sections 65864 thru 65869.5 authorizes the City of Morgan Hill to enter into binding Development Agreements with persons having legal or equitable interests in real property for the development of such property.

SECTION 3. The Planning Commission, pursuant to Title 18, Chapter 18.78.125 of the Municipal Code and Resolution No. 04-038, adopted April 13, 2004, has awarded allotments to a certain project herein after described as follows:

<u>Project</u>	<u>Total Dwelling Units</u>
MMP-03-06: DeWitt-Latala	4 Single-Family Homes

SECTION 4. References are hereby made to certain Agreements on file in the office of the City Clerk of the City of Morgan Hill. These documents to be signed by the City of Morgan Hill and the property owner set forth in detail and development schedule, the types of homes, and the specific restrictions on the development of the subject property. Said Agreement herein above referred to shall be binding on all future owners and developers as well as the present owners of the lands, and any substantial change can be made only after further public hearings before the Planning Commission and the City Council of this City.

SECTION 5. The City Council hereby finds that the development proposal and agreement approved by this ordinance is compatible with the goals, objectives, policies, and land uses designated by the General Plan of the City of Morgan Hill.

SECTION 6. Authority is hereby granted for the City Manager to execute all development agreements approved by the City Council during the Public Hearing Process.

SECTION 7. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 8. Effective Date Publication. This ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

SECTION 9. The approved project shall be subject to the conditions as identified in the set of standard conditions attached hereto, as exhibit "A", and by this reference incorporated herein.

The foregoing ordinance was introduced at the regular meeting of the City Council of the City of Morgan Hill held on the 6th Day of October 2004, and was finally adopted at a regular meeting of said Council on the 20th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: COUNCIL MEMBERS:
NOES: COUNCIL MEMBERS:
ABSTAIN: COUNCIL MEMBERS:
ABSENT: COUNCIL MEMBERS:

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

⌘ CERTIFICATE OF THE CITY CLERK ⌘

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. , New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the 20th Day of October 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

ZONING AMENDMENT, ZAA-03-13: CITY OF MORGAN HILL – ATTACHED HOUSING ZONING TEXT AMENDMENT

RECOMMENDED ACTION(S):

1. Open/close Public Hearing
2. Waive the First and Second Reading of Ordinance
3. Introduce Ordinance

EXECUTIVE SUMMARY: In November 2003, the City Council adopted Ordinance No. 1641 (attached) to allow single-family attached (duet) units to be split into two detached units on separate lots with a minimum building separation of three feet and a maximum separation of six feet. The “Modified Setback Ordinance” was adopted in response to the high cost of obtaining construction liability insurance for attached housing units. This ordinance allows the modified setback dwellings to be constructed for residential projects awarded a building allocation in FY 2003-04 and 2004-05. Under Section 15 of the attached ordinance, the modified setbacks may be extended for Measure P projects awarded a building allotment in FY 2005-06 and to FY 2006-07 units that are issued building permits by June 30, 2006. Section 20 of the Ordinance provides at the end of 12 months after enactment of the Ordinance, the Planning Commission shall hold hearings to review the progress and status of the modified setback dwellings. The Commission would then forward a recommendation to the City Council to either extend or terminate this Ordinance at the end of the two year term.

Although the one year review period of the current ordinance will not occur until November, the City Council, at their June 21, 2004 meeting, determined that the need for a modified setback ordinance will continue beyond November 2004 because of the continuing high cost of construction liability insurance. The Council agreed to consider an early application to extend Ordinance 1641. On July 29, 2004, an application to extend the ordinance was filed by local developers Richard Oliver, Scott Schilling and Rocke Garcia. The Planning Commission considered the ordinance amendment request at their September 14 and September 28 meetings and voted 6-0 to recommend the two year extension.

In addition to the extension of time, the Planning Commission is recommending that Section 11 of Ordinance 1641 be amended to allow a side yard fence to be constructed at the centerline of the six foot separation of the modified setback units. The current Ordinance has a provision that requires a primary “use” easement be recorded allowing the owner of one dwelling full use of the six foot side yard that represents the separation between the two units. Allowing the fence to be centered between the two units on the property line creates two three foot side yards instead of one zero and the one six foot yard, but eliminates the need for the primary and secondary access easements. The Planning Commission recommends allowing the narrower side yards provided the three foot section extends no more than 50 percent of the length of the side of the building. The attached ordinance extends the term to the Modified Setback Ordinance (Ord.1641) for an additional two year term. Section 3 of this ordinance amends the fence placement requirement as outlined above. The Commission reports and minutes are also attached.

FISCAL IMPACT: No budget adjustment required.

Agenda Item # 19

Prepared By:

Planning Manager

Submitted By:

City Manager

ORDINANCE NO. _____, NEW SERIES

**AN ORDINANCE OF THE CITY COUNCIL OF THE CITY
OF MORGAN HILL EXTENDING AND MODIFYING
ORDINANCE 1641 ALLOWING MODIFIED SETBACK
DWELLINGS IN RESIDENTIAL PROJECTS DUE TO
CONSTRUCTION LIABILITY INSURANCE ISSUES
SURROUNDING OWNERSHIP ATTACHED HOUSING**

WHEREAS, a goal of the Morgan Hill General Plan is to provide “a variety of housing types and densities available to all residents”; and,

WHEREAS, a goal of the Morgan Hill Affordable Housing Strategy is to provide a variety of housing for all income levels, specifically housing for moderate income levels; and,

WHEREAS, attached housing, including BMR units, provide housing opportunities for all income levels, but specifically for low and moderate income levels; and,

WHEREAS, construction liability insurance for projects with ownership attached housing continues to be unavailable to many local contractors and subcontractors; and,

WHEREAS, construction liability insurance for projects with ownership attached housing continues to be difficult to obtain and cost prohibitive for local developers; and,

WHEREAS, the insurance issue continues to impede Morgan Hill developers from fulfilling their Residential Development Control System (RDCS) commitments to provide below market rate (BMR) housing and attached housing in Morgan Hill; and,

WHEREAS, the Home Builders’ Association continues to work with the California Legislature to develop solutions to the insurance crisis relating to attached housing; and,

WHEREAS, as an alternative to attached housing, local developers requested the enactment of an ordinance to allow construction of modified setback dwellings, or dwellings physically separated but architecturally connected by a design element to give the appearance of attachment; and,

WHEREAS, modified setback dwellings will provide greater architectural continuity in neighborhoods consisting primarily of detached dwellings; and,

WHEREAS, the separation of attached units will allow for the addition of architectural features such as windows, which will enhance the appearance of the homes and improve the function of the interior spaces; and,

WHEREAS, the City reviewed all other alternatives to such ordinance, including a no action alternative, and determined that an ordinance allowing modified setback dwellings was the feasible solution to prevent significant delays in the construction of new housing in Morgan Hill; and,

WHEREAS, following a duly noticed public hearing the City Council adopted Ordinance 1641 on November 5, 2003; and,

WHEREAS, should insurance products for attached housing become reasonably available again due to action of the California Legislature, Ordinance 1641 was enacted for a limited time period; and,

WHEREAS, the limited time period of Ordinance 1641 presents problems for RDSC applicants who are designing projects for time periods beyond the life span of Ordinance 1641, and thus are not sure whether to design attached or detached housing; and,

WHEREAS, in order to address this concern and assure consistency in RDSC competitions, the City Council deems it appropriate to extend Ordinance 1641, and apply its provisions to current RDSC competitions; and,

WHEREAS, in order to ensure design consistency in projects which are phased in through multiple RDSC competitions, it is advisable to allow projects which have approved detached housing products for which RDSC allocations are awarded, either pursuant to Ordinance 1641 or this Ordinance, to continue to have that detached product throughout the project; and,

WHEREAS, testimony and exhibits received at a noticed public hearing having been duly considered,

NOW, THEREFORE, THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY ORDAIN AS FOLLOWS:

SECTION 1. The findings of Ordinance 1641 are hereby incorporated as if set forth herein in their entirety.

SECTION 2. Section 10 of Ordinance 1641 is hereby amended to provide:

“This Ordinance hereby allows developers to build modified setback dwellings in lieu of standard attached dwellings, subject to the following eligibility criteria:

a. Only *projects for which Measure P RDSC* allotments *were* awarded for Fiscal Year ~~2004-05~~ *2006-07* and earlier, and *also* allotments for which building permits are issued by June 30, ~~2005~~ *2007* are eligible for the modified setback dwellings, except as provided in Sections 15 through 19 of this Ordinance.”

SECTION 3. Section 11 of Ordinance 1641 is hereby amended to provide:

“Modified setback dwellings shall be designed to comply with the following design standards:

a. Duet units – a zero *or three foot* side yard setback is allowed on one side of one of the duet units.

- b. Single-family Attached Housing Consisting of Three Units - zero ***or three foot*** side yard setbacks are allowed on both sides of the center unit and on the outer side yards of the end units.
- c. Single-family Attached Housing Consisting of Four or More Units - lots for each unit shall be designed large enough to accommodate a zero ***or three foot*** setback on one side and a minimum three-ft setback on the other side.
- d. Minimum separation between dwellings shall be three feet.
- e. Maximum separation between dwellings shall be six feet, except as allowed under subparagraph (f), below.
- f. A maximum separation between adjacent dwellings shall not be required for modified setback dwellings on alternative lot configurations, such as z-lots or lots with off-set property lines, provided that the adjacent dwellings give the appearance of attachment from the public right-of-way.
- g. Side yard setbacks adjacent to single-family detached dwellings shall be a minimum of five feet.
- h. The side yard setback along the side street property line of a corner lot shall be a minimum of 15 feet.
- i. In no case shall front or rear yard setbacks be reduced to less than 20 feet in depth, unless previously approved by the City Council as part of an RPD Overlay District.
- j. Architectural treatment, such as a wing wall, trellis, staggered fireplaces along the separated wall of both units, or other similar treatment, shall be provided in between modified setback dwellings to give the appearance of attachment, although, the units will be physically detached.
- k. Should a fence be constructed between the modified setback dwellings, a gate shall be provided allowing access from the front yard to the side yard area.
- l. Eaves and overhangs may encroach over property lines, subject to compliance with building code standards and provided appropriate easements and Covenant, Conditions & Restrictions (CC&Rs) are recorded.
- m. A deed restriction shall be recorded over every modified setback lot prohibiting future building additions on either side of the homes, unless the additions comply with the site development standards of the underlying zoning district.
- n. For adjacent dwellings with minimum three-ft and maximum six-ft separations ***and where a zero setback is established for one of the units,*** primary access and exclusive use of the adjoining side yard area shall be granted to the property owner with the greater side yard width. ~~In cases of equal side yard widths, the RPD shall identify to which property owner primary access and exclusive use is granted.~~ Secondary access shall be granted to the adjacent property owner for maintenance of the exterior wall. An easement shall be recorded over the adjoining side yard area granting access to the adjacent property owner for maintenance of the exterior wall, and CC&Rs shall be recorded granting the exclusive and reasonable use of the adjoining side yard area to the

appropriate property owner, with restrictions to minimize potential conflicts. ***Primary and secondary easements shall not be required in cases of equal side yard widths where a six foot building separation and three foot side yard is provided and the fence is located along the common property line. The three foot side yard area shall extend no more than 50 percent of the length of the side of the building.***

- o. A closed pipe system providing positive drainage shall be provided between modified setback dwellings.
- p. Rain gutters connected to a closed pipe drainage system shall be provided for all modified setback dwellings. CC&Rs shall be recorded requiring property owners to maintain rain gutters to minimize impacts to the adjacent property(ies).
- q. Modified setback dwellings shall be designed in full compliance with 2001 ~~Uniform~~ **California** Building Codes.
- r. All projects containing modified setback dwellings shall have an approved RPD Overlay Zoning.

SECTION 4. Section 15 of Ordinance 1641 is hereby amended to provide:

“This Ordinance may be extended to allow modified setback dwellings for ***projects for which Measure P RDCS*** allotments ~~were~~ awarded for Fiscal Year ~~2005-06~~ **2007-08**, and ***also*** allotments for which building permits are issued by June 30, ~~2006~~ **2008**, subject to the approval of the City Council.”

SECTION 5. Section 16 of Ordinance 1641 is hereby amended to provide:

“Projects ~~with~~ ***for which Measure P RDCS*** allotments ~~were~~ awarded for Fiscal Year ~~2004-05~~ **2006-07**, and ***also*** allotments for which building permits are issued by June 30, ~~2005~~ **2007** shall be subject to the requirements listed below. Should the City Council extend this Ordinance, allotments awarded for Fiscal Year ~~2005-06~~ **2007-08** and allotments for which building permits are issued by June 30, ~~2006~~ **2008** shall also be subject to the following requirements:”

SECTION 6. Projects which meet the following criteria may continue to incorporate single-family modified setback dwellings, as defined in Municipal Code section 18.04.156, beyond the expiration or termination date of Ordinance 1641 and this Ordinance, if such projects meet the following criteria:

- a. The project is to be constructed in multiple phases, all of which are shown on a ~~Measure P RDCS~~ application submitted within the time frame of this Ordinance; and,
- b. The project receives ~~Measure P RDCS~~ allocations in the 2004-05, 2005-06, or 2006-07 competitions.

SECTION 7. This Ordinance and Ordinance 1641 shall automatically expire and be of no further force and effect at the end of twenty-four (24) months after the date of this Ordinance, unless extended by the City Council with appropriate findings and resolutions.

SECTION 8. The Council, upon appropriate findings, may revoke this Ordinance and Ordinance 1641 prior to the expiration of the Ordinance. If no action is taken by the City Council, the Ordinance shall remain in effect until its expiration date.

SECTION 9. Severability. If any part of this Ordinance is held to be invalid or inapplicable to any situation by a court of competent jurisdiction, such decision shall not affect the validity of the remaining portions of this Ordinance or the applicability of this Ordinance to other situations.

SECTION 10. Effective Date; Publication. This ordinance shall take effect from and after thirty (30) days after the date of its adoption. The City Clerk is hereby directed to publish this ordinance pursuant to §36933 of the Government Code.

The foregoing ordinance was introduced at the regular meeting of the City Council of the City of Morgan Hill held on the th Day of October 2004, and was finally adopted at a regular meeting of said Council on the th Day of October 2004, and said ordinance was duly passed and adopted in accordance with law by the following vote:

AYES: **COUNCIL MEMBERS:**
NOES: **COUNCIL MEMBERS:**
ABSTAIN: **COUNCIL MEMBERS:**
ABSENT: **COUNCIL MEMBERS:**

ATTEST:

APPROVED:

Irma Torrez, City Clerk

Dennis Kennedy, Mayor

∞ CERTIFICATE OF THE CITY CLERK ∞

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Ordinance No. _____, New Series, adopted by the City Council of the City of Morgan Hill, California at their regular meeting held on the th Day of October, 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk



CITY COUNCIL STAFF REPORT

MEETING DATE: October 6, 2004

Agenda Item # 20

**Recommended and
Submitted By:**

Dennis Kennedy, Mayor

LIVESTOCK REGULATIONS

RECOMMENDED ACTION(S): Request the Planning Commission to consider revisions to the livestock regulations in residential and commercial zones

EXECUTIVE SUMMARY: Section 6.36.050 of the Municipal Code (attached) restricts the number of livestock that may be maintained on property within residential and/or commercial zones.

The regulations prohibit any number of livestock on parcels less than one acre, and provide for a maximum of two (2) livestock and their immature offspring on larger parcels, unless the Council specifically approves a higher number upon a finding of no detriment to abutting property owners. The permit requires payment of an application fee.

There has been recent press attention to a code enforcement case in which the lessee of a parcel of residentially zoned property was maintaining for a third party more than the permitted number of animals.

I recommend that Council ask the Planning Commission to consider appropriate revisions to the ordinance so as to permit a larger number of animals on larger parcels without the need for a separate permit.

FISCAL IMPACT: NONE



JOINT CITY COUNCIL/ REDEVELOPMENT AGENCY STAFF REPORT

MEETING DATE: October 6, 2004

LEASE WITH THE CALIFORNIA YOUTH SOCCER ASSOCIATION (CYSA)

Agenda Item # 21

Approved By:

BAHS Director

Submitted By:

Executive Director

RECOMMENDED ACTION(S): Provide parameters for negotiating a lease extension with CYSA to continue using the future location of the sports complex as a CYSA regional soccer complex.

EXECUTIVE SUMMARY:

In July 2001, the Redevelopment Agency purchased the 35 acre site commonly known as the regional soccer complex located on Condit Road between San Pedro and Barrett Avenues. The site is currently being leased to CYSA for use as a regional soccer complex. The current lease with CYSA expires December 31, 2004. CYSA is responsible for all maintenance and repair of the facility as well as all utility costs.

CYSA is inquiring about a lease extension for next year. This will allow them time to make other arrangements should the facility be unavailable for their use. CYSA is not proposing any other amendments at this time. Before negotiating an extension with CYSA, we would like direction from the Agency on three key issues: 1) whether an extension is acceptable and for how long and 2) whether the construction of the parking lot is negotiable as to size and, location, and 3) whether the existing terms are acceptable. Some key issues to consider in your discussions are:

- CYSA states any extension would need to be a minimum of ten months because most of their field use occurs from July thru October 2005.
- The Parks and Recreation Commission will be reporting back to the Council in November with a recommendation regarding improvements for Phase I of the sports complex. If approved by the Agency, staff anticipates we could begin construction in Fall 2005. About 8-10 months will be needed to design and bid out the improvements.
- The San Jose Soccer Complex Foundation anticipates being able to complete its new regional soccer complex on the "Sobrato" property sometime in 2006.
- The current lease rate is \$25,259.50 adjusted annually based on the CPI.
- Under the current agreement, the Agency may use the facility twice a week from June to November for recreational programming.
- The Agency is considering the construction of a parking lot on the soccer complex to provide overflow parking for the Aquatics Center. This parking lot would eliminate one soccer field as it would be located on the field nearest the Aquatics Center. CYSA is currently evaluating the impact the loss of one field will have on its operations.

Based on the above factors, it would appear that a ten month extension would not impact the plans for the City's sports complex.

FISCAL IMPACT: n/a



CITY COUNCIL & MORGAN HILL FINANCING AUTHORITY STAFF REPORT

Agenda Item # 22

Prepared By:

Finance Director

Submitted By:

City Manager

MEETING DATE: *October 6, 2004*

ISSUANCE OF BONDS FOR WATER PROJECTS

RECOMMENDED ACTIONS:

1. As City Council, adopt Resolution approving as to form and authorizing the execution and delivery of certain documents in connection with the sale and issuance of Morgan Hill Financing Authority water revenue bonds.
2. As Authority Commission of the Financing Authority, adopt Resolution authorizing the issuance, sale, and delivery of water revenue bonds and approving certain documents.
3. Authorize the City Manager, on behalf of the City, to enter into agreements with RBC Dain Rauscher Inc. for financial advisory services and with Richards, Watson & Gershon for bond counsel/disclosure counsel services.

EXECUTIVE SUMMARY: The Financing Authority plans to issue water revenue bonds in order to raise the funds necessary to allow the City to finance approximately \$6.5 million in various water capital improvement projects, including certain costs already incurred.

Under the proposed financing structure, the City will purchase Facilities from the Financing Authority and make certain installment payments to the Authority which will be sufficient to enable the Authority to make debt service payments to bondholders.

Working with RBC Dain Rauscher, the City's Financial Advisor, staff will take steps to obtain bond insurance, if the purchase of such insurance will result in lower interest costs sufficient to cover the cost of the insurance. In addition, the Financial Advisor will proceed to conduct a competitive bond sale under which these bonds will be sold to the bidders with the lowest effective interest rates.

FISCAL IMPACT: Under the Authority Resolution, the bond issue will not exceed \$8,000,000 and the interest rate will not exceed 5.75%. However, it is expected that the bond issue will be sized at \$7.52 million and that the net interest rate will be 4.75%. It is estimated that the net annual debt service for this new bond issuance will be \$341,000 through 2021 and that, when added to the existing 1999 certificates of participation issue payments, the combined net debt service for both water related bond issues will total \$725,000 per year through 2021, at which time the 1999 issue will be paid off. Subsequently, annual debt service on the new bond issue will be approximately \$765,000 for years 2022 through 2034. Approximately 30% of the annual debt service for the new bond issue will be paid by the water operations fund and the remaining 70% through the water development impact fund.

SUMMARY OF ATTACHMENTS

Attachment

- | | |
|---|---|
| 1) City Council Resolution approving certain documents and issuance of Authority bonds | A |
| 2) Financing Authority Resolution authorizing the sale, issuance, and delivery of bonds and approving certain documents | B |
| 3) Installment Sales Agreement between City and Financing Authority | C |
| 4) Official Notice Inviting Bids for purchase of bonds | D |
| 5) Trust Agreement between Financing Authority and BNY Western Trust Company | E |
| 6) Preliminary Official Statement | F |
| 8) Agreement with Richards, Watson & Gershon for bond counsel/disclosure counsel services | G |
| 9) Agreement with RBC Dain Rauscher Inc. for financial advisory services | H |

RESOLUTION NO. _____

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MORGAN HILL APPROVING AS TO FORM AND AUTHORIZING THE EXECUTION AND DELIVERY OF CERTAIN DOCUMENTS IN CONNECTION WITH THE SALE AND ISSUANCE OF MORGAN HILL FINANCING AUTHORITY WATER REVENUE BONDS, SERIES 2004 AND AUTHORIZING CERTAIN OTHER MATTERS RELATING THERETO

RECITALS:

WHEREAS, the Morgan Hill Financing Authority (the “Authority”) proposes to sell its Water Revenue Bonds, Series 2004 (the “Series 2004 Bonds”), in an aggregate principal amount not exceeding \$8,000,000; and

WHEREAS, proceeds from the sale of the Series 2004 Bonds will be used to finance certain capital improvements for the production, storage or transmission of water (the “Project”) in the City of Morgan Hill (the “City”); and

WHEREAS, the Authority is a joint powers authority duly organized and existing under and pursuant to Articles 1 through 4 (commencing with Section 6500), Chapter 5, Division 7, Title 1 of the California Government Code (the “Act”) and a Joint Exercise of Powers Agreement, dated as of November 3, 2003, by and between the City and the Morgan Hill Redevelopment Agency; and

WHEREAS, under the Act, the Authority is authorized to borrow money for the purpose of financing certain public capital improvements for the benefit of the City, including facilities for the production, storage or transmission of water; and

WHEREAS, in connection with the issuance Series 2004 Bonds, the City and the Authority propose to enter into an Installment Sale Agreement (the “Installment Sale Agreement”), under which the City will agree to make certain installment payments to be calculated such that such payments will be sufficient to enable the Authority to pay debt service on the Series 2004 Bonds;

NOW, THEREFORE, THE CITY COUNCIL OF THE CITY OF MORGAN HILL DOES HEREBY RESOLVE, DETERMINE AND ORDER AS FOLLOWS:

Section 1. Recitals. The above recitals, and each of them, are true and correct.

Section 2. Installment Sale Agreement. The Installment Sale Agreement proposed to be entered into by and between the City and the Authority, in the form presented at this meeting and on file in the office of the City Clerk, is hereby approved. Each of the Mayor (or in his absence, the Mayor Pro Tem) and the City Manager of the City (each, an “Authorized Officer”), acting singly, is hereby authorized and directed, for and in the name and on behalf of the City, to execute and deliver the Installment Sale Agreement in substantially said form, with such changes

therein as the Authorized Officer executing the same may approve (such approval to be conclusively evidenced by such Authorized Officer's execution and delivery thereof).

Section 3. Continuing Disclosure Agreement. The Continuing Disclosure Agreement (the "Continuing Disclosure Agreement"), proposed to be entered into by and between the City and BNY Western Trust Company, as the Trustee and Dissemination Agent, in the form presented at this meeting and on file in the office of the City Clerk, is hereby approved. Each Authorized Officer, acting singly, is hereby authorized and directed, for and in the name and on behalf of the City, to execute and deliver the Continuing Disclosure Agreement in substantially said form, with such changes therein as the Authorized Officer executing the same may approve (such approval to be conclusively evidenced by such Authorized Officer's execution and delivery thereof).

Section 4. Preliminary Official Statement. The Preliminary Official Statement relating to the Series 2004 Bonds (the "Preliminary Official Statement"), in the form presented at this meeting and on file with the City Clerk, is hereby approved. Each Authorized Officer, acting singly, is hereby authorized and directed, for and in the name and on behalf of the City, to cause the Preliminary Official Statement in substantially said form, with such additions or changes therein as such Authorized Officer may approve, to be deemed final for the purposes of Rule 15c2-12 of the Securities and Exchange Act of 1934. The distribution of the Preliminary Official Statement to prospective bidders of the Series 2004 Bonds pursuant to the Authority's resolution approving the issuance of the Series 2004 Bonds is hereby approved.

Section 5. Official Statement. Each Authorized Officer, acting singly, is hereby authorized and directed, for and in the name and on behalf of the City, to cause the Preliminary Official Statement to be brought into the form of a final Official Statement (the "Official Statement"), and to execute the same for and in the name and on behalf of the City, with such additions or changes therein as such Authorized Officer may approve (such approval to be conclusively evidenced by such Authorized Officer's execution and delivery thereof).

Section 6. Appointments of Bond Counsel and Financial Advisor. The appointments of Richards, Watson & Gershon, A Professional Corporation, to serve as Bond Counsel and RBC Dain Rauscher Inc. to serve as Financial Advisor with respect to the financing contemplated herein, are hereby approved.

Section 7. Other Acts. The Authorized Officers and all other officers of the City are hereby authorized and directed, jointly and severally, to do any and all things, to execute and deliver any and all documents that they may deem necessary or advisable in order to consummate the sale, issuance and delivery of the Series 2004 Bonds, or otherwise to effectuate the purposes of this Resolution, the Installment Sale Agreement, the Official Statement and the Continuing Disclosure Agreement and any such actions previously taken by such officers are hereby ratified and confirmed.

Section 8. Effective Date. This Resolution shall take effect immediately upon adoption.

PASSED AND ADOPTED by the City Council of Morgan Hill at a Regular Meeting held on the th Day of October, 2004 by the following vote.

AYES: **COUNCIL MEMBERS:**
NOES: **COUNCIL MEMBERS:**
ABSTAIN: **COUNCIL MEMBERS:**
ABSENT: **COUNCIL MEMBERS:**

☪ CERTIFICATION ☪

I, IRMA TORREZ, CITY CLERK OF THE CITY OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Resolution No. , adopted by the City Council at a Regular Meeting held on October , 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, City Clerk

RESOLUTION NO. MHFA-__

**A RESOLUTION OF THE MORGAN HILL FINANCING AUTHORITY
AUTHORIZING THE ISSUANCE, SALE AND DELIVERY OF ITS
WATER REVENUE BONDS, SERIES 2004; APPROVING AS TO FORM
AND AUTHORIZING THE EXECUTION AND DELIVERY OF A TRUST
AGREEMENT, AN INSTALLMENT SALE AGREEMENT, AND
CERTAIN OTHER DOCUMENTS IN CONNECTION THEREWITH;
AND AUTHORIZING CERTAIN OTHER MATTERS RELATING
THERE TO**

RECITALS:

WHEREAS, the Morgan Hill Financing Authority (the “Authority”) is a joint powers authority duly organized and existing under and pursuant to Articles 1 through 4 (commencing with Section 6500), Chapter 5, Division 7, Title 1 of the California Government Code (the “Act”) and that certain Joint Exercise of Powers Agreement, dated as of November 5, 2003, by and between the City of Morgan Hill (the “City”) and the Morgan Hill Redevelopment Agency, and is authorized pursuant to Article 4 of the Act to issue bonds for the purpose of financing public capital improvements; and

WHEREAS, the Authority proposes to sell Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 (the “Series 2004 Bonds”) to be issued and secured pursuant to an Trust Agreement (as defined herein); and

WHEREAS, proceeds from the sale of the Series 2004 Bonds will be used to finance certain capital improvements for the production, storage or transmission of water (the “Project”) in the City of Morgan Hill (the “City”); and

WHEREAS, in connection with the issuance of the Series 2004 Bonds, the City and the Authority propose to enter into (a) an Installment Sale Agreement (the “Installment Sale Agreement”), whereby the City will make certain installment payments to be calculated such that such payments will be sufficient to enable the Authority to pay the principal of, and interest and premium (if any) on, such bonds when due;

NOW, THEREFORE, THE MORGAN HILL FINANCING AUTHORITY DOES HEREBY RESOLVE, DETERMINE AND ORDER AS FOLLOWS:

Section 1. Recitals. The above recitals, and each of them, are true and correct.

Section 2. Issuance of Bonds. The Authority hereby authorizes the issuance of bonds in one or more series, in an aggregate principal amount not exceeding \$8,000,000, to provide funds to finance the Project. The bonds shall be designated the “Morgan Hill Financing Authority Water Revenue Bonds, Series 2004” (the “Series 2004 Bonds”) and shall be issued in accordance with the Act and the terms and conditions set forth in the Trust Agreement (defined below).

Section 3. Trust Agreement. The Trust Agreement (the “Trust Agreement”), proposed to be entered into by and between the Authority and the Trustee (defined in Section 4 below), in the form presented at this meeting and on file with the Secretary of the Authority (the “Authority Secretary”), is hereby approved. Subject to Section 6 below, each of the President, the Vice President, the Chief Administrative Officer and the Treasurer, any deputy of such officers, and any member of the Authority Commission (each, an “Authorized Officer”), acting singly, is hereby authorized and directed, for and in the name and on behalf of the Authority, to execute and deliver the Trust Agreement in substantially said form, with such additions or changes as the Authorized Officer executing the same may approve (such approval to be conclusively evidenced by such Authorized Officer’s execution and delivery thereof).

Section 4. Appointment of Trustee. The appointment of BNY Western Trust Company as trustee (the “Trustee”) under the Trust Agreement is hereby approved.

Section 5. Installment Sale Agreement. The Installment Sale Agreement (the “Installment Sale Agreement”), proposed to be entered into by and between the City and the Authority, in the form presented at this meeting and on file in the office of the Secretary of the Authority, is hereby approved. Each Authorized Officer, acting singly, is hereby authorized and directed, for and in the name and on behalf of the Authority, to execute and deliver the Installment Sale Agreement in substantially said form, with such changes therein as the Authorized Officer executing the same may approve (such approval to be conclusively evidenced by such Authorized Officer’s execution and delivery thereof).

Section 6. Terms of Sale of Bonds. The authorization set forth in this Resolution regarding the issuance and sale of the Series 2004 Bonds are subject to the following parameters: (i) the aggregate principal amount of the Series 2004 Bonds shall not exceed \$8,000,000; (ii) interest rate on the Series 2004 Bonds shall not exceed 5.75 percent per annum; and (iii) the underwriter’s discount with respect to the Series 2004 Bonds shall not exceed 2.0 percent of the principal amount thereof. In addition, the authorization and powers delegated to the Authorized Officers by Section 7 shall be valid for a period of 180 days from the date of adoption of this Resolution.

Section 7. Notice Inviting Bids. The Official Notice Inviting Bids (the “Notice Inviting Bids”), in the form presented at this meeting and on file in the office and on file with the Secretary of the Authority, is hereby approved. Each Authorized Officer, acting singly, is hereby authorized, for and in the name of the Authority, to use the Notice Inviting Bids, with such changes, insertions and omissions as such Authorized Officer may require or approve, to solicit from underwriters proposals to purchase the Series 2004 Bonds. Subject to the parameters set forth in Section 6 hereof, the terms and conditions of the offering and sale of the Series 2004 Bonds shall be as specified in the Notice Inviting Bids. Sealed bids for the purchase of the Series 2004 Bonds shall be received by the Authority at the time and place set forth in the Notice Inviting Bids. The Authorized Officers are each hereby authorized and directed, for and in the name of the City, to accept the lowest bid for the Series 2004 Bonds, or to reject all bids therefor, in accordance with the Notice Inviting Bids.

Section 8. Appointment of Bond Counsel and Financial Advisor. The Authority hereby approves the appointment of Richards, Watson & Gershon, A Professional Corporation, to serve as Bond Counsel and RBC Dain Rauscher Inc. to serve as Financial Advisor with respect to the financing contemplated herein.

Section 9. Preliminary Official Statement. The Preliminary Official Statement relating to the Series 2004 Bonds (the "Preliminary Official Statement"), in the form presented at this meeting and on file with the Authority Secretary, is hereby approved. Each Authorized Officer, acting singly, is hereby authorized and directed, for and in the name and on behalf of the Authority, to cause the Preliminary Official Statement in substantially said form, with such additions or changes therein as such Authorized Officer may approve, to be deemed final for the purposes of Rule 15c2-12 of the Securities and Exchange Act of 1934. The Authorized Officers are hereby authorized and directed to furnish, or cause to be furnished, to prospective bidders for the Series 2004 Bonds, a reasonable number of copies of the Preliminary Official Statement.

Section 10. Official Statement. Each Authorized Officer, acting singly, is hereby authorized and directed, for and in the name and on behalf of the Authority, to cause the Preliminary Official Statement to be brought into the form of a final Official Statement (the "Official Statement"), and to execute the same for and in the name and on behalf of the Authority, with such additions or changes therein as such Authorized Officer may approve (such approval to be conclusively evidenced by such Authorized Officer's execution and delivery thereof). The Authorized Officers are each hereby authorized and directed to furnish or cause to be furnished, to the purchaser of the Series 2004 Bonds, as many copies of the Official Statement as said purchaser shall require, provided that no charge shall be imposed on the first 75 copies of the Official Statement.

Section 11. Other Acts. The Authorized Officers and all other officers of the Authority are hereby authorized and directed, jointly and severally, to do any and all things (including the negotiating and obtaining of a municipal bond insurance policy with respect to the Bonds), to execute and deliver any and all documents that they may deem necessary or advisable in order to consummate the sale, issuance and delivery of the Series 2004 Bonds, or otherwise to effectuate the purposes of this Resolution, the Trust Agreement, the Installment Sale Agreement, the Notice Inviting Bids and the Official Statement and any such actions previously taken by such officers are hereby ratified and confirmed.

Section 12. Effective Date. This Resolution shall take effect immediately upon adoption.

PASSED AND ADOPTED by the Morgan Hill Financing Authority Commission at a Special Meeting held on the th Day of October, 2004 by the following vote.

AYES: COMMISSION MEMBERS:
NOES: COMMISSION MEMBERS:
ABSTAIN: COMMISSION MEMBERS:
ABSENT: COMMISSION MEMBERS:

COMMISSION PRESIDENT

ATTEST:

COMMISSION SECRETARY

🦉 CERTIFICATION 🦉

I, IRMA TORREZ, SECRETARY OF THE MORGAN HILL FINANCING AUTHORITY COMMISSION OF MORGAN HILL, CALIFORNIA, do hereby certify that the foregoing is a true and correct copy of Resolution No. MHFA-, adopted by the Authority Commission at a Special Meeting held on October , 2004.

WITNESS MY HAND AND THE SEAL OF THE CITY OF MORGAN HILL.

DATE: _____

IRMA TORREZ, Commission Secretary

INSTALLMENT SALE AGREEMENT

by and between the

MORGAN HILL FINANCING AUTHORITY

and the

CITY OF MORGAN HILL

Dated as of October 1, 2004

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INSTALLMENT SALE AGREEMENT

THIS INSTALLMENT SALE AGREEMENT, dated as of October 1, 2004 (this "Installment Sale Agreement"), between the MORGAN HILL FINANCING AUTHORITY, a joint powers authority duly organized and existing under the laws of the State of California (the "Authority"), as seller, and the CITY OF MORGAN HILL, a municipal corporation duly organized and existing under the laws of the State of California (the "City"), as purchaser.

W I T N E S S E T H:

WHEREAS, the Authority is a joint powers authority duly organized and existing under and pursuant to Articles 1 through 4 (commencing with Section 6500) of Chapter 5 of Division 7 of Title 1 of the California Government Code (the "Act") and a Joint Exercise of Powers Agreement, dated as of November 5, 2003, by and between the City and the Morgan Hill Redevelopment Agency; and

WHEREAS, under the Act, the Authority is authorized to borrow money for the purpose of financing certain public capital improvements of the City, including facilities for the production, storage, transmission or treatment of water; and

WHEREAS, the City operates a water system (such system, including all additions, improvements and extensions thereto, the "Water System") to serve the City; and

WHEREAS, the Authority desires to assist the City with respect to the financing of certain additions, improvements and extensions to the Water System; and

WHEREAS, for the purpose of providing funds to the City, the Authority has authorized the issuance of its Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 (the "Series 2004 Bonds") pursuant to the Trust Agreement, dated as of even date herewith, by and between the Authority and BNY Western Trust Company, as Trustee; and

WHEREAS, in furtherance of the above described financing, the City and the Authority desire to enter into this Installment Sale Agreement, pursuant to which the City shall purchase the Facilities (as defined below) from the Authority and make certain installment payments which have been calculated to be sufficient to enable the Authority to pay the principal of and interest and premium, if any, on the Series 2004 Bonds when due and payable; and

WHEREAS, the Authority and the City have duly authorized the execution and delivery of this Installment Sale Agreement;

NOW, THEREFORE, for and in consideration of the premises and the material covenants hereinafter contained, the parties hereto hereby formally covenant, agree and bind themselves as follows:

ARTICLE I

DEFINITIONS AND EXHIBITS

SECTION 1.01. Definitions. The following terms shall, for all purposes of this Installment Sale Agreement, have the respective meanings ascribed to them in this Section 1.01. All capitalized terms used in this Installment Sale Agreement which are not defined herein but are defined in the Trust Agreement shall have the meanings specified in the Trust Agreement.

“Accountant” shall mean any independent certified public accountant or firm of such accountants selected by the City.

“Acquisition and Construction” means, with respect to any of the Facilities, the acquisition, construction, improvement, equipment, renovation, remodeling and/or reconstruction thereof.

“Additional Payments” means the amounts payable by the City pursuant to Section 3.03.

“Annual Debt Service” means, with respect to Installment Payments and Parity Obligations, and with respect to any Bond Year during the Term of this Installment Sale Agreement, the sum obtained by totaling the following amounts for such Bond Year:

- (a) the aggregate amount of the Installment Payments coming due and payable in such Bond Year pursuant hereto, except to the extent payable from any escrow deposit pursuant to Section 9.01;
- (b) the principal amount of all outstanding Parity Obligations, if any, coming due and payable by their terms in such Bond Year; and
- (c) the amount of interest which would be due during such Bond Year on the aggregate principal amount of all outstanding Parity Obligations, if any, which would be outstanding in such Bond Year if such Parity Obligations are retired as scheduled.

“Event of Default” means any of the events described in Section 8.01.

“Facilities” means the facilities and improvements described in Exhibit A attached hereto and by this reference incorporated herein.

“Fiscal Consultant” means any consultant or firm of such consultants appointed by the Authority and the City and who, or each of whom: (a) is judged by the Authority and the City to have experience in matters relating to the financing of water system enterprises; (b) is in fact independent and not under domination of the Authority or the City; (c) does not have any substantial interest, direct or indirect, with the Authority or the City other than as purchaser of the Bonds or any Parity Obligations; and (d) is not connected with the Authority or the City as an officer or employee of the Authority or the City, but who may be regularly retained to make reports to the Authority or the City.

“Gross Revenues” means all income, rents, rates, fees, charges and other moneys derived from the ownership or operation of the Water System, including, without limiting the generality of the foregoing, (i) all income, rents, rates, fees, charges, business interruption insurance proceeds or other moneys derived by the City from the sale, furnishing and supplying of the water or other services, facilities, and commodities sold, furnished or supplied through the facilities of or in the conduct or operation of the business of the Water System, (ii) the earnings on and income derived from the investment of such income, rents, rates, fees, charges, or other moneys, including City reserves, (iii) the proceeds of any stand—by or water availability charges collected by the City, and (iv) the proceeds of any facilities fees or connection fees collected by the City, but excluding in all cases (A) customers’ deposits or any other deposits or advances subject to refund until such deposits or advances have become the property of the City, (B) any proceeds of taxes restricted by law to be used by the City to pay bonds hereafter issued, and (C) revenues from any surcharge that have been designated by the City for use for specific purposes, including with limitation, the perchlorate-related surcharge imposed pursuant to Resolution No. 5766, adopted by the City Council on February 4, 2004.

“Independent Accountant” means any certified public accountant or firm of certified public accountants appointed and paid by the City, and who, or each of whom: (a) is in fact independent and not under domination of the City or the Authority; (b) does not have any substantial interest, direct or indirect, in the City or the Authority; and (c) is not connected with the City or the Authority as an officer or employee of the City or the Authority but who may be regularly retained to make annual or other audits of the books of or reports to the City or the Authority.

“Installment Payment Date” means the first day of each June 1 and December 1 during the Term of this Installment Sale Agreement, commencing June 1, 2005.

“Installment Payments” means the amounts payable by the City pursuant to Section 3.01 and Exhibit C hereto, including any prepayments thereof pursuant to Section 3.02.

“Installment Sale Agreement” means this Installment Sale Agreement, together with any duly authorized and executed amendments hereto.

“Maximum Annual Debt Service” means, as of the date of any calculation and with respect to the Installment Payments and any Parity Obligations, the maximum sum obtained for the current or any future Bond Year during the Term of this Installment Sale Agreement by totaling the following amounts for each such Bond Year:

(a) the aggregate amount of the Installment Payments coming due and payable in such Bond Year pursuant hereto, except to the extent payable from any escrow deposit pursuant to Section 9.01;

(b) the principal amount of all outstanding Parity Obligations, if any, coming due and payable by their terms in such Bond Year; and

(c) the amount of interest which would be due during such Bond Year on the aggregate principal amount of all outstanding Parity Obligations, if any,

which would be outstanding in such Bond Year if such Parity Obligations are retired as scheduled.

“Net Proceeds” means, with respect to any condemnation award or with respect to any insurance proceeds, the amount of such condemnation award or such insurance proceeds remaining after payment of all expenses (including attorneys’ fees) incurred in the collection of such award or proceeds.

“Net Revenues” means, for any period, an amount equal to all of the Gross Revenues received during such period minus the amounts required to pay all Operation and Maintenance Costs and the 1999 Installment Payments becoming payable during such period.

“1999 Installment Payments” means the “Installment Payments” payable by the City under the 1999 Installment Purchase Agreement.

“1999 Installment Purchase Agreement” means that certain Installment Purchase Agreement, dated as of May 1, 1999, by and between the City and the Morgan Hill Wastewater Facilities Financing Corporation, as the same may be amended or supplemented from time to time in accordance with the terms thereof.

“Operation and Maintenance Costs” means the reasonable and necessary costs paid or incurred by the City for maintaining and operating the Water System, determined in accordance with generally accepted accounting principles, including all reasonable expenses of management and repair and all other expenses necessary to maintain and preserve the Water System in good repair and working order, and including all administrative costs of the City that are charged directly or apportioned to the operation of the Water System, such as salaries and wages of employees, overhead, taxes (if any), the cost of permits and licenses to operate the Water System and insurance premiums, and including all other reasonable and necessary costs of the City or charges required to be paid by it to comply with the terms hereof; but excluding in all cases (i) depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles, and (ii) any costs covered by revenues from surcharges described in clause (C) of the definition of “Gross Revenues.”

“Parity Obligations” means the 2003 Loan and any leases, loan agreements, installment sale agreements, bonds, notes or other obligations of the City payable from and secured by a pledge of and lien upon any of the Net Revenues on a parity with the Installment Payments, entered into or issued pursuant to and in accordance with Section 5.01.

“Series 2004 Bonds” means “Morgan Hill Financing Authority Water Revenue Bonds, Series 2004,” issued pursuant to the Trust Agreement.

“Series 2004 Bonds Closing Date” means the date of original issuance of the Series 2004 Bonds.

“Term” means, with respect to this Installment Sale Agreement, the time commencing on the Series 2004 Bonds Closing Date and ending on the date the City shall have paid or prepaid all of the Installment Payments hereunder in accordance with Article III or IX.

“Trust Agreement” means the Trust Agreement, dated as of even date herewith, by and between the Authority and BNY Western Trust Company, as Trustee, and as the same may be further amended or supplemented from time to time.

“2004 Project Costs” means the costs, expenses and liabilities paid or incurred or to be paid or incurred by the City or the Authority, all calculated in accordance with generally accepted accounting principles, in connection with acquisition(s), financing, planning, engineering, design, construction and installation(s) relating to the 2004 Projects or any portion thereof, and the obtaining of all governmental approvals, certificates, permits and licenses with respect thereto, including but not limited to (a) the costs of acquisition or construction by or for the City of real and personal property or any interest therein, (b) any good faith or other similar payment or deposits, (c) the costs of any demolitions or relocation necessary in connection therewith, (d) costs of physical construction and costs incidental to such construction or acquisition, (e) all costs relating to injury and damage claims, (f) the costs of any indemnity or surety bonds and premiums on insurance, including obligations to a stock, mutual or reciprocal insurance company or exchange, (f) preliminary investigation and development costs, (g) engineering fees, contractors’ fees, legal fees and expenses, and any other fees and expenses of professional consultants and (h) the costs of labor, materials, equipment and utility services and supplies, (i) administrative and general overhead expenses and costs of keeping accounts and making reports required by the Trust Agreement prior to or in connection with the completion of the 2004 Projects, (j) all federal, state and local taxes and payments in lieu of taxes legally required to be paid in connection with the 2004 Projects prior to or in connection with the completion of the 2004 Projects. It is intended that this definition of 2004 Project Costs be broadly construed to encompass all costs, expenses and liabilities of the City and the Authority which are chargeable to the capital accounts of the 2004 Projects in accordance with generally accepted accounting principles.

“2004 Projects” means the 2004 Projects described in Exhibit B attached hereto and by this reference incorporated herein.

“2003 Loan” means the loan made by the Authority to the City pursuant to the 2003 Loan Agreement.

“2003 Loan Agreement” means the Loan Agreement, dated as of December 1, 2003, by and between the City and the Authority, and as the same may be amended or supplemented from time to time pursuant to the terms thereof.

“Water Revenue Fund” means the “City of Morgan Hill Water Revenue Fund” heretofore established and held by the City with respect to the Water System, as further described in Section 4.02.

“Water System” means the whole and each and every part of the water system of the City, including the portion thereof existing on the date hereof, and including all additions, betterments, extensions and improvements to such water system or any part thereof hereafter acquired or constructed; provided, that to the extent the City is not the sole owner of an asset or property or to the extent that an asset or property is used in part for the above described water system purposes, only the City’s ownership interest in such asset or property or only the part of

the asset or property so used for water system purposes shall be considered to be part of the Water System.

SECTION 1.02. Construction; Interpretation. The headings or titles of the several Articles and Sections hereof, and any table of contents appended to copies hereof, shall be solely for convenience of reference and shall not affect the meaning, construction or effect of this Installment Sale Agreement. All references herein to “Articles,” “Sections” and other subsections are to the corresponding Articles, Sections or subsections of this Installment Sale Agreement; the words “herein,” “hereof,” “hereby,” “hereunder” and other words of similar import refer to this Installment Sale Agreement as a whole and not to any particular Article, Section or subsection hereof; and words of the masculine gender shall mean and include words of the feminine and neuter genders. Words in the singular shall include the plural and words in the plural shall include the singular where the context so requires.

ARTICLE II

ISSUANCE OF SERIES 2004 BONDS; CONSTRUCTION AND SALE OF FACILITIES; ASSIGNMENT TO TRUSTEE

SECTION 2.01. Issuance of Series 2004 Bonds. The Authority has authorized the issuance of the Series 2004 Bonds in the aggregate principal amount of _____ Dollars (\$_____) pursuant to the Trust Agreement, for the purpose of providing funds to finance certain capital costs relating to the 2004 Projects. The Authority agrees that the proceeds of sale of the Series 2004 Bonds shall be paid to the Trustee on the Series 2004 Bonds Closing Date for deposit pursuant to the terms and conditions of the Trust Agreement. The City hereby approves the Trust Agreement, the assignment to the Trustee of the rights of the Authority assigned thereunder, and the issuance of the Bonds by the Authority pursuant thereto.

SECTION 2.02. Construction of Facilities; Appointment of City as Agent.
(a) In consideration for the issuance of the Series 2004 Bonds and the application of the proceeds pursuant hereto and to the Trust Agreement, the City hereby grants, assigns and transfers to the Authority, all estate, right, title and interest of the City in the Facilities, and the Authority accepts the same from the City.

(b) The Authority hereby agrees with due diligence to cause the Acquisition and Construction of the Facilities in accordance with billing statements, contracts and documents relating thereto and approved by the City pursuant to all applicable requirements of law. The Authority expects that the portion of the Acquisition and Construction of the Facilities to be financed with proceeds from the sale of the Series 2004 Bonds will be completed by the third anniversary of the issuance date of the Series 2004 Bonds; provided, however, that the failure to complete any Facilities by such date shall not constitute an Event of Default hereunder or grounds for termination hereof, nor shall such failure result in the diminution, abatement or extinguishment of the obligations of the City hereunder to pay the Installment Payments allocable to such Facilities.

(c) The City hereby grants to the Authority all necessary easements, rights of way and rights of access in and to all real property or interests therein now or hereafter acquired or owned by the City, as may be necessary or convenient to enable the Authority to comply with subsection (b) above. The City covenants that it will execute, deliver and record any and all additional documents as may be required or appropriate to be executed, delivered and/or recorded to establish such easements, rights of way and rights of access.

(d) The Authority hereby appoints the City as its agent to carry out all phases of the Acquisition and Construction of the Facilities pursuant to and in accordance with the provisions hereof. The City hereby accepts such appointment and assumes all rights, liabilities, duties and responsibilities of the Authority regarding the Acquisition and Construction of the Facilities. The City, as agent of the Authority hereunder, is hereby authorized to and shall enter into and, administer and enforce all purchase orders or other contracts relating to the Acquisition and Construction of the Facilities.

SECTION 2.03. Purchase of Facilities by City. Subject and pursuant to the terms of this Installment Sale Agreement, the Authority hereby sells, assigns and transfers, and the City hereby purchases, all of the Authority's right, title and interest in the Facilities to the City. To pay the purchase price therefor, the City agrees to make Installment Payments in the manner set forth in this Installment Sale Agreement. The parties hereto agree that all rights, title and interest of the Authority in the Facilities shall be deemed reconveyed, reassigned and vested in the City upon earlier of (a) the date of completion of the Acquisition and Construction of the Facilities, (b) the date on which the Series 2004 Bonds shall have been paid in full or provision for their payment has been made in accordance with the Trust Agreement.

SECTION 2.04. Assignment to Trustee. The City understands and agrees that all Installment Payments and all of the rights of the Authority in this Installment Sale Agreement (other than the rights of the Authority under Sections 3.03, 7.02 and 8.04 hereof) have been assigned by the Authority to the Trustee in trust, pursuant to the Trust Agreement, for the benefit of the Owners of the Bonds, and the City hereby assents to such assignment. The Authority hereby directs the City, and the City hereby agrees, to pay to the Trustee at its Corporate Trust Office, in immediately available funds, all amounts payable by the City pursuant to this Section 2.04 and all amounts payable by the City pursuant to Sections 3.01 and 3.02 and Article IX.

ARTICLE III

INSTALLMENT PAYMENTS; PREPAYMENTS; ADDITIONAL PAYMENTS

SECTION 3.01. Installment Payments. The City shall, subject to any rights of prepayment hereinafter provided, pay to the Authority, or its successors and assigns, but solely from the Net Revenues and other funds pledged hereunder, Installment Payments as purchase price for the Facilities. The Installment Payments shall become due and payable in the amounts and on the respective dates specified in Exhibit C hereto. The Installment Payments shall be paid by the City to the Trustee (as assignee of the Authority), in the amounts and at the times as set forth in Section 4.02.

SECTION 3.02. Optional Prepayment. (a) The City may prepay, at its sole option and from any source of available funds, the principal components, in whole or in part (but only in \$5,000 integrals), on any date on or after June 1, 20__, of unpaid Installment Payments becoming due and payable on or after June 1, 20__. Such prepayment price shall be applied by the Trustee to redeem Series 2004 Bonds pursuant to Section 4.01(b) of the Trust Agreement. In the event of such a prepayment, the City shall pay a prepayment price equal to the sum of the following: (i) the aggregate principal components of the Installment Payments to be prepaid, (ii) the interest components of the Installment Payments required to be paid on or accrued to such date, [and (iii) a prepayment premium equal to the redemption premium payable pursuant to Section ____ of the Trust Agreement upon redemption of the Series 2004 Bonds being called as the result of such prepayment.]

The City shall give the Trustee written notice of its intention to exercise its option to prepay pursuant to this Section 3.02(a) not less than forty-five (45) days in advance of the date of exercise and shall specify in such notice (i) the amount of the principal component of the Installment Payments the City intends to prepay and (ii) the intended date of prepayment.

(c) Upon delivery of the notice of prepayment to the Trustee described in the Section 3.02(a), the City shall deliver such prepayment price to the Trustee for deposit in the Interest Account and the Redemption Fund within the period prescribed under the Trust Agreement; provided, that the City may, in its discretion, rescind any optional prepayment pursuant to Section 3.02(a) by notifying the Authority and providing a written notice to the Trustee on or before the date fixed for prepayment.

(d) Upon a prepayment by the City of Installment Payments in part but not in whole pursuant to subsection (a) above and the corresponding redemption of Series 2004 Bonds pursuant to Section 4.01(b) of the Trust Agreement, the principal and interest components of succeeding Installment Payments, shall be reduced to correspond with the principal and interest amounts payable with respect to the remaining unredeemed portion of Series 2004 Bonds.

SECTION 3.03. Additional Payments. In addition to the Installment Payments, the City shall pay when due all costs and expenses incurred by the Authority to comply with the provisions of this Installment Sale Agreement and the Trust Agreement, including without limitation all Costs of Issuance (to the extent not paid from amounts deposited in the Costs of Issuance Fund). The City shall also pay to the Trustee, upon request therefor, all

compensation for fees due to the Trustee and all of its costs and expenses payable as a result of its performance in accordance with the Trust Agreement, this Installment Sale Agreement or any related documents, together with all amounts required to indemnify the Trustee pursuant to Section 7.03 hereof or Section 9.04 of the Trust Agreement. The rights of the Trustee and the obligations of the City under this Section 3.03 shall survive the termination of this Installment Sale Agreement.

SECTION 3.04. Rate on Overdue Payments. In the event the City should fail to make any of the payments required in this Article III, the payment in default shall continue as an obligation of the City until the amount in default shall have been fully paid, and the City agrees to pay the same with interest thereon, from the date of default to the date of payment, at the same rate of interest otherwise payable on the Bonds.

ARTICLE IV

PLEDGE OF NET REVENUES; WATER REVENUE FUND; SERIES 2004 PROJECT ACCOUNT

SECTION 4.01. Pledge of Net Revenues. All of the Net Revenues and all moneys on deposit in any of the funds and accounts established under the Trust Agreement (other than any fund established exclusively to hold money for the payment of arbitrage rebate in order to comply with the Tax Certificate and the Code) are hereby irrevocably pledged, charged and assigned to the punctual payment of the Installment Payments and, except as otherwise provided herein, the Net Revenues and such other funds shall not be used for any other purpose so long as any of the Installment Payments remain unpaid. Such pledge, charge and assignment shall constitute a first lien on the Net Revenues and moneys for the payment of amounts due with respect to the Installment Payments and Parity Obligations in accordance with the terms hereof and thereof.

The obligations of the City to make the Installment Payments and the Additional Payments from the Net Revenues and to perform and observe the other agreements contained herein shall be absolute and unconditional and shall not be subject to any defense or any right of setoff, counterclaim or recoupment arising out of any breach of the City, the Authority or the Trustee of any obligation to the City or otherwise with respect to the Water System, whether hereunder or otherwise, or out of indebtedness or liability at any time owing to the City by the Authority or the Trustee. Until such time as all of the Installment Payments and all of the Additional Payments coming due and payable hereunder shall have been fully paid or prepaid, the City (a) will not suspend or discontinue payment of any Installment Payments, Additional Payments or such other amounts, (b) will perform and observe all other agreements contained in this Installment Sale Agreement, and (c) will not terminate this Installment Sale Agreement for any cause, including, without limiting the generality of the foregoing, the occurrence of any acts or circumstances that may constitute failure of consideration, eviction or constructive eviction, destruction of or damage to the Water System, sale of any portion of the Water System, the taking by eminent domain of title to or temporary use of any component thereof, commercial frustration of purpose, any change in the tax law or other laws of the United States of America or

the State or any political subdivision of either thereof or any failure of the Authority or the Trustee to perform and observe any agreement, whether express or implied, or any duty, liability or obligation arising out of or connected with the Trust Agreement or this Installment Sale Agreement.

The City's obligation to pay the Installment Payments and the Additional Payments shall be a special obligation of the City limited solely to the Net Revenues. Under no circumstances shall the City be required to advance moneys derived from any source of income other than the Net Revenues and other sources specifically identified in this Installment Sale Agreement and the Trust Agreement for the payment of the Installment Payments and the Additional Payments, nor shall any other funds or property of the City be liable for the payment of the Installment Payments and the Additional Payments and any other amounts coming due and payable hereunder and under the Trust Agreement. Neither the Authority nor the Trustee nor any Owner shall have the right, directly or indirectly, to require or compel the exercise of the *ad valorem* taxing power of the City or the forfeiture of any property of the City, including the Water System, for the making of any payments hereunder.

SECTION 4.02. Water Revenue Fund. (a) The City has heretofore established a fund designated as the "City of Morgan Hill Water Revenue Fund" (the "Water Revenue Fund") and has held and shall continue to hold such fund segregated from all other funds of the City. All Gross Revenues shall be deposited by the City immediately upon receipt in the Water Revenue Fund and shall be applied, first, to pay Operation and Maintenance Costs as they become due and payable (including amounts reasonably required to be set aside in contingency reserves for Operation and Maintenance Costs, the payment of which is not then immediately required). The City may at any time establish such sub-level funds and accounts as it deems necessary or desirable within the Water Revenue Fund. The City covenants and agrees that all Net Revenues shall be held by the City in the Water Revenue Fund in trust for the benefit of the Trustee (as assignee of the Authority pursuant to the Trust Agreement) and the Bond Owners, and for the benefit of the owners of any Parity Obligations.

(b) No later than five (5) Business Days before each Installment Payment Date, the City shall withdraw from the Water Revenue Fund and transfer to the Trustee, for deposit in the Bond Fund, an amount which, together with the balance then on deposit in the Bond Fund (other than (i) amounts resulting from the prepayment of the Installment Payments pursuant to Article IX and (ii) amounts required for payment of principal of or interest on any Bonds which have matured or been called for redemption but which have not been presented for payment) is equal to the aggregate amount of the Installment Payments coming due and payable on such Installment Payment Date.

(c) No later than five (5) Business Days before each Installment Payment Date, the City shall pay to the Trustee the amount of any deficiency in the Reserve Account, the notice of which deficiency shall have been given by the Trustee to the City pursuant to Section 5.09 of the Trust Agreement.

(d) In addition to Operation and Maintenance Costs and amounts to be transferred to the Trustee under (b) and (c) above, the City shall withdraw from the Water

Revenue Fund such amounts at such times as shall be required to pay: (i) the 1999 Installment Payments as the same shall become due and payable, (ii) the principal of and interest on any Parity Obligations and otherwise comply with the provisions of the instruments authorizing the issuance of any Parity Obligations; and (iii) all other amounts when and as due and payable hereunder.

(e) The City shall manage, conserve and apply the Net Revenues on deposit in the Water Revenue Fund in such a manner that all deposits required to be made pursuant to the preceding subsections (b), (c) and (d) will be made at the times and in the amounts so required. Subject to the foregoing sentence, so long as no Event of Default shall have occurred and be continuing hereunder, the City may use and apply moneys in the Water Revenue Fund for (i) the payment of Additional Payments, (ii) the payment of any subordinate obligations or any unsecured obligations, (iii) the costs for additional improvements, extensions, replacements and betterments to the Water System, (iv) the prepayment of any obligations of the City relating to the Water System, or (v) any other lawful purposes of the City.

(f) Any moneys held in the Water Revenue Fund shall be invested in Permitted Investments which will, as nearly as practicable, mature on or before the dates when such moneys are anticipated to be needed for disbursement hereunder. All investment earnings from moneys or deposits in the Water Revenue Fund shall be credited in such fund and applied only to the purposes permitted for such fund. The City may commingle any of the moneys in the Water Revenue Fund with the moneys held in other funds and accounts (except for moneys held in any rebate fund which shall be held separately) for investment purposes; provided, however, that all moneys in the Water Revenue Fund shall be accounted for separately notwithstanding such commingling.

SECTION 4.03. Series 2004 Project Account. The City, may from time to time, deliver a Written Requisition of the City to the Trustee to withdraw money from the Series 2004 Project Account and transfer such money to or on the order of the City to pay the 2004 Projects Costs. Any such Written Requisition of the City shall be in the form prescribed in Section 5.03 of the Trust Agreement. The City shall maintain on file a record of all expenditures of such moneys withdrawn from the Series 2004 Project Account, including all Written Requisitions of the City and records evidencing the person to whom payment is to be made, the amount of money to be paid, the purpose for which the obligation to be paid was incurred and that such payment was a proper charge against the Series 2004 Project Account and has not been the subject of previous Written Requisitions of the City. After the completion of all of the 2004 Projects, the City shall promptly notify the Authority and shall, in writing, notify the Trustee of such completion and specify to the Trustee the portion, if any, of the remaining balance in the Series 2004 Project Account which shall be applied to a payment or prepayment of Installment Payments under Section 3.02 hereof and the applicable payment or prepayment date. If, pursuant to the previous sentence, the City elects to instruct the Trustee to apply all or a portion of the remaining balance in the Series 2004 Project Account to the optional prepayment of Installment Payments, the City shall deliver a written notice to the Trustee of such optional prepayment in accordance with Section 3.02 hereof.

ARTICLE V

ADDITIONAL PARITY OBLIGATIONS

SECTION 5.01. Conditions for Incurrence of Additional Parity Obligations.

(a) Subject to the conditions set forth in this Section 5.01, the Authority and the City from time to time may amend this Installment Sale Agreement to increase or adjust the Installment Payments in connection with the issuance of Additional Bonds pursuant to Article VI of the Trust Agreement and the City from time to time may issue or incur additional Parity Obligations. Any issuance by the Authority of Additional Bonds or any incurrence by the City of Parity Obligations is subject to the following conditions:

(i) The City shall be in compliance with all covenants in this Installment Sale Agreement;

(ii) No Event of Default hereunder and no event of default under the 1999 Installment Sale Agreement or with respect to any Parity Obligations shall have occurred and be continuing; and

(iii) The Net Water Revenues, together with any available property tax revenues, received by the City in the most recent Fiscal Year for which audited financial statements are available, shall be at least equal to 120 percent of the sum of the Maximum Annual Debt Service with respect to the 1999 Installment Payments (as defined in the 1999 Installment Sale Agreement) plus the Maximum Annual Debt Service with respect to the Installment Payments hereunder and any Parity Obligations which will be outstanding immediately following the incurrence of such Parity Obligations, as evidenced by a Report of an Independent Accountant or Fiscal Consultant;

(iv) If required by the terms of such Parity Obligation, a separate reserve has been or will be established therefor and that provisions have been made to fund such reserve.

(b) The foregoing conditions of Section 5.01(a) shall not apply to, or in any way limit, the City's ability to incur Parity Obligations at any time to refund any outstanding Installment Payments or Parity Obligations, if such refunding will result in a net present value savings to the City (inclusive of all costs of such refunding).

SECTION 5.02. Superior and Subordinate Obligations. (a) So long as any Bonds issued under the Trust Agreement remain Outstanding, the City shall not issue or incur any additional bonds or other obligations, which will rank senior in the priority of lien over the Installment Payments with respect to the Net Revenues.

(b) Nothing in this Installment Sale Agreement shall be construed to limit or affect the ability of the City to issue or incur obligations which are either unsecured or which rank junior to the Installment Payments in their lien with respect to the Net Revenues.

ARTICLE VI

OTHER COVENANTS OF CITY

SECTION 6.01. Compliance with Agreement. The City shall punctually pay the Installment Payments in strict conformity with the terms hereof, and shall faithfully observe and perform all the agreements, conditions, covenants and terms contained herein required to be observed and performed by it. The City shall not fail to make any Installment Payment required by this Installment Sale Agreement for any cause including, without limiting the generality of the foregoing, any acts or circumstances that may constitute failure of consideration, destruction of or damage to all or a portion of the Water System, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State or any political subdivision of either or any failure of the Authority to observe or perform any agreement, condition, covenant or term contained in this Installment Sale Agreement required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected with this Installment Sale Agreement or the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Authority or any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lockouts, lack of transportation facilities, fire, explosion, or acts or regulations of governmental authorities.

SECTION 6.02. Distribution of Net Revenues for Debt Service. The City hereby covenants that the City will distribute Net Revenues available for outstanding Installment Payments and debt service on all outstanding Parity Obligations on a *pro rata* basis without regard to whether each such Parity Obligation has a funded debt service reserve or a surety bond or other similar funding instrument.

SECTION 6.03. Rates and Charges. (a) The City shall fix, prescribe, revise and collect rates, fees and charges for the services and facilities furnished by the Water System during each Fiscal Year, which are at least sufficient, after making allowances for contingencies and error in the estimates, to yield Gross Revenues which are sufficient to pay the following amounts in the following order of priority:

(i) All Operation and Maintenance Costs estimated by the City to become due and payable in such Fiscal Year;

(ii) The 1999 Installment Payments as they become due and payable during such Fiscal Year;

(iii) The Installment Payments and the principal of and interest on then Outstanding Parity Obligations as they become due and payable during such Fiscal Year, without preference or priority (except to the extent such Installment Payments or such principal and interest on Parity Obligations are payable from the proceeds of the Bonds or Parity Obligations, or from any other source of legally available funds of the City which have been deposited with the Trustee for such purpose prior to the commencement of such Fiscal Year);

(iv) All amounts, if any, required to restore the balance in the Reserve Account to the full amount of the Reserve Requirement; and

(v) All Additional Payments and other payments required to meet any other obligations of the City which are charges, liens, encumbrances upon, or which are otherwise payable, from Gross Revenues during such Fiscal Year.

(b) In addition, the City shall fix, prescribe, revise and collect rates, fees and charges for the services and facilities furnished by the Water System during each Fiscal Year, so that Gross Revenues less Operation and Maintenance Costs will be at least equal to 120 percent of the sum of the amounts described in the preceding clause (a)(ii) and clause (a)(iii) of this Section.

(c) The City will have in effect at all times rules and regulations requiring each consumer or customer located on any premises connected with the Water System to pay the rates and charges applicable to the Water System provided to such premises and providing for the billing thereof and for a due date and a delinquency date for each bill.

SECTION 6.04. Maintenance and Operation of the Water System. The City will maintain and preserve the Water System in good repair and working order at all times and will operate the Water System in an efficient and economical manner and will pay all Operation and Maintenance Costs as they become due and payable.

SECTION 6.05. Tax Covenants. (a) The City hereby covenants it shall not take any action, or fail to take any action, if any such action or failure to take action would adversely affect the Tax-exempt status of the interest on the Bonds under Section 103 of the Code. Without limiting the generality of the foregoing, the City shall comply with the requirements of the Tax Certificate, which is incorporated herein as if fully set forth herein.

(b) In the event that at any time the City is of the opinion that, in order to comply with its obligations under subsection (a) of this Section, it is necessary or helpful to restrict or limit the yield on the investment of any moneys in any of the funds or accounts held by the Trustee pursuant to the Trust Agreement, the City shall so notify the Authority and the Authority then shall promptly instruct the Trustee in writing, and cause the Trustee to take such action as may be necessary in accordance with such instructions.

(c) The City agrees to furnish all information to, and cooperate fully with, the Authority, the Trustee and their respective officers, employees, agents and attorneys, in order to assure compliance with the provisions of Section 7.03 of the Trust Agreement. In the event that the Authority shall determine, pursuant to Section 7.03 of the Trust Agreement, that any amounts are due and payable to the United States of America thereunder and that neither the Authority nor the Trustee has on deposit an amount of available moneys (excluding moneys on deposit in the funds and accounts established for the payment of the principal of or interest or redemption premium, if any, on the Bonds) to make such payment, the Authority shall promptly notify the City of such fact. Upon receipt of any such notice, the City shall promptly pay to the Trustee from any source of legally available funds the amounts determined by the Authority to be due and payable to the United States of America under Section 7.03 of the Trust Agreement.

The covenants in this Section shall survive payment in full or discharge of the Installment Payments and the Bonds.

SECTION 6.06. Insurance. The City shall procure and maintain such insurance relating to the Water System (including the Facilities) which it shall deem advisable or necessary to protect its interests and the interests of the Authority, which insurance shall afford protection in such amounts and against such risks as are usually covered in connection with public water systems similar to the Water System; provided, that any such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and manner as is, in the opinion of an accredited actuary, actuarially sound. If all or any part of the Water System shall be taken by eminent domain proceedings, or if the City receives any insurance proceeds resulting from a casualty loss to the Water System, subject to the provisions of the 1999 Installment Purchase Agreement, the Net Proceeds (after application thereof pursuant to the 1999 Installment Purchase Agreement, if any of the 1999 Installment Payments remains outstanding at such time) may be used, at the option of the City, to (a) repair, rebuild or replace such damaged, destroyed or taken portion of the Water System, or (b) prepay Installment Payments or any Parity Obligations.

SECTION 6.07. Payment of Taxes and Compliance with Governmental Regulations. The City will pay and discharge all taxes, assessments and other governmental charges which may hereafter be lawfully imposed upon the Water System or any part thereof when the same shall become due. The City will duly observe and conform with all valid regulations and requirements of any governmental authority relative to the operation of the Water System or any part thereof, but the City shall not be required to comply with any regulations or requirements so long as the validity or application thereof shall be contested in good faith and contesting such validity or application will not materially impair the operations or financial condition of the Water System.

SECTION 6.08. Sale or Other Disposition of Property. The City will not sell, transfer or otherwise dispose of any of the works, plant, properties, facilities or other part or rights of the Water System or any real or personal property comprising a part of the Water System if such sale, transfer or disposition would cause the City to be unable to satisfy the requirements of Section 6.03 hereof.

SECTION 6.09. Compliance with Contracts; Liens. The City shall not commit any breach or default under any agreement affecting or involving the Water System (to the extent that the City is a party thereto), or permit any lien to be attached to any portion of the Water, if such breach, default, or lien which would materially adversely affect its ability to comply with its covenants set forth in Section 6.03 hereof.

SECTION 6.10 Accounting Records; Financial Statements and Other Reports. The City will keep appropriate accounting records in which complete and correct entries shall be made of all transactions relating to the Water System. The City will prepare and file with the Trustee annually within one hundred eighty (180) days after the close of each Fiscal Year (commencing with the Fiscal Year ending June 30, 2005), the following: (a) audited financial statements of the Water System for such Fiscal Year prepared in accordance with generally accepted accounting principles, together with a report thereon by and Independent

Accountant, (b) a report as to all insurance policies maintained and self-insured programs maintained by the City with respect to the Water System, as of the close of such Fiscal Year, including the names of the insurers which have issued the policies and the amounts thereof and the property or risks covered thereby, (c) a summary report showing in reasonable detail, the amounts of Gross Revenues, Net Revenues and the Operation and Maintenance Costs for such Fiscal Year, and containing a general description of the Water System.

ARTICLE VII

LIABILITY OF AUTHORITY; INDEMNIFICATION OF AUTHORITY AND TRUSTEE

SECTION 7.01. Non-Liability of Authority. The Authority shall not be obligated to pay Installment Payments or the principal, and premium, if any, and interest with respect to the Bonds from any moneys other than Revenues.

SECTION 7.02. Indemnification of Authority. The City agrees, to the extent permitted by law, to indemnify, defend and hold harmless the Authority and its directors, officers, employees and agents from and against any and all losses, claims, damages, liabilities or expenses, of every kind, character and nature whatsoever, including, but not limited to, losses, claims, damages, liabilities, or expenses arising out of, resulting from or in any way connected with (a) the Facilities or the 2004 Projects or the acquisition, condition, use or possession thereof or any part thereof; (b) the issuance and delivery of any Bonds and the carrying out of any of the transactions contemplated by this Installment Sale Agreement or the Trust Agreement; or (c) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading in any official statement or other offering circular utilized in connection with the sale of the Bonds. The City further agrees, to the extent permitted by law, to pay or to reimburse the Authority and its officers, employees and agents for any and all costs, reasonable attorneys fees, liabilities or expenses incurred in connection with investigating, defending against or otherwise in connection with any such losses, claims, damages, liabilities, expenses or actions. However, the City shall not hold harmless or indemnify the Authority, its directors and officers for any losses which are caused by the bad faith or willful misconduct of the Authority, its directors or officers.

SECTION 7.03. Trustee Expenses; Indemnification of Trustee . (a) The City covenants and agrees to (i) pay the Trustee from time to time, and the Trustee shall be entitled to receive, reasonable compensation (which shall not be limited by any provision of law in regard to the compensation of a trustee of an express trust), and (ii) pay or reimburse the Trustee upon request for all reasonable expenses, disbursements and advances incurred or made in accordance with any of the provisions of this Installment Sale Agreement and the Trust Agreement (including the reasonable compensation, expenses and disbursements of its counsel and of all agents and other persons not regularly in its employ).

(b) The City covenants and agrees to pay and to indemnify the Trustee, and to hold it harmless against, any loss, liability or expense incurred by it, arising out of or in connection with the acceptance or administration of the Trust Agreement or the trusts thereunder or the performance of its duties hereunder or under the Trust Agreement, including the costs and

expenses of defending itself against or investigating any claim of liability in the premises, except to the extent that any such loss, liability or expense arose from the Trustee's own gross negligence or bad faith. The City shall have the right to select any attorneys employed pursuant to this Section 7.03(b); provided, however, that if the City fails to select attorneys pursuant to this Section 7.03(b) after notice from the Trustee, the Trustee may select such attorneys.

SECTION 7.04. Survive Termination. The provisions of this Article shall survive payment in full of the Installment Payments and the Bonds, the expiration of the Trust Agreement and the termination of this Installment Sale Agreement.

ARTICLE VIII

DEFAULTS AND REMEDIES

NOTWITHSTANDING ANYTHING TO THE CONTRARY IN THIS ARTICLE VIII, SO LONG AS THE BOND INSURANCE POLICY REMAINS IN EFFECT AND THE BOND INSURER HAS NOT DEFAULTED WITH RESPECT TO ITS OBLIGATIONS UNDER THE BOND INSURANCE POLICY, ALL PROVISIONS OF THIS ARTICLE XI SHALL BE SUBJECT TO, AND QUALIFIED BY, THE PROVISIONS SET FORTH IN ARTICLE X HEREOF.

SECTION 8.01. Events of Default; Acceleration.

If one or more of the following events (each, an "Event of Default") shall occur:

(a) If the City shall fail to pay in full any Installment Payment pursuant to Section 3.01 hereof at the time and in the manner specified herein;

(b) If the City shall fail to observe or perform any covenant, condition, agreement or provision in this Installment Sale Agreement on its part to be observed or performed, other than as referred to in subsection (a) of this Section 8.01, or shall breach any warranty by the City herein contained, for a period of thirty (30) days after written notice, specifying such failure or breach and requesting that it be remedied, has been given to the City by the Authority or the Trustee; except that if such failure or breach can be remedied but not within such thirty (30) day period and if the City has taken all action reasonably possible to remedy such failure or breach within such thirty (30) day period, such failure or breach shall not become an Event of Default for so long as the City shall diligently proceed to remedy same in accordance with and subject to any directions or limitations of time established by the Authority or the Trustee, as the case may be;

(c) If an "Event of Default" as defined in the Trust Agreement shall have occurred under the Trust Agreement;

(d) If the City files a petition in voluntary bankruptcy, for the composition of its affairs or for its corporate reorganization under any state or federal bankruptcy or insolvency law, or makes an assignment for the benefit of creditors, or admits in writing to its insolvency or inability to pay debts as they mature, or consents in writing to the appointment of a trustee or

receiver for itself or for the whole or any substantial part of the Water System;

(e) If a court of competent jurisdiction shall enter an order, judgment or decree declaring the City an insolvent, or adjudging it bankrupt, or appointing a trustee or receiver of the City or of the whole or any substantial part of the Water System, or approving a petition filed against the City seeking reorganization of the City under any applicable law or statute of the United States of America or any state thereof, and such order, judgment or decree shall not be vacated or set aside or stayed within thirty (30) days from the date of the entry thereof; or

(f) If, under the provisions of any other law for the relief or aid of debtors, any court of competent jurisdiction shall assume custody or control of the City, and such custody or control shall not be terminated within thirty (30) days from the date of assumption of such custody or control;

then and in each and every such case during the continuance of such Event of Default specified in clause (d), (e) or (f) above, the Authority shall, and for any other such Event of Default the Authority may, by notice in writing to the City, declare the entire amount of the unpaid Installment Payments coming due to and including the date of such declaration to be due and payable immediately, and upon any such declaration the same shall become immediately due and payable, anything contained herein to the contrary notwithstanding.

This Section is subject to the condition, however, that the Authority, by written notice to the City, may rescind and annul such declaration and its consequences if at any time after such declaration and before any judgment or decree for the payment of the money due shall have been obtained or entered, the following shall have occurred: (i) the City shall have transferred to the Trustee for deposit in the Bond Fund a sum sufficient to pay the unpaid amount of the Installment Payments due as a result of such declaration, (ii) the City shall have deposited, or caused to be deposited, in the applicable debt service fund(s) the unpaid principal amount of any payments due under any Parity Obligation referred to in clause (a) above due and payable prior to such declaration and the accrued interest thereon, (iii) the City shall have paid the reasonable expenses of the Authority, the Trustee and any fiduciaries for Parity Obligations resulting from such declaration, and (iv) any and all other defaults known to the Authority (other than in the payment of the entire amount of the unpaid Installment Payments due and payable solely by reason of such declaration) shall have been made good or cured to the satisfaction of the Authority or provision deemed by the Authority to be adequate shall have been made therefor. The City acknowledges that the Authority's exercise of a rescission and annulment in one instance shall not extend to and shall not affect any subsequent default, and shall not impair or exhaust any right or power consequent thereon.

SECTION 8.02. Allocation of Funds Upon Acceleration Upon the date of the declaration of acceleration as provided in Section 8.01, all Revenues thereafter received by the City shall be applied in the following order:

First, to the payment, without preference or priority, and in the event of any insufficiency of such Revenues ratably without any discrimination or preference, of the fees,

costs and expenses of the Authority and Trustee, if any, in carrying out the provisions of this Article, including reasonable compensation to their respective accountants and counsel;

Second, to the payment of Operation and Maintenance Costs;

Third, to the payment of the entire principal amount of the unpaid Installment Payments and the unpaid amount of all Parity Obligations and the accrued interest thereon, with interest on overdue installments at the rate or rates of interest applicable to the Installment Payments and such Parity Obligations if paid in accordance with their respective terms; and

Fourth, to the payment of all amounts owed to the Bond Insurer other than amounts paid under the preceding paragraph.

SECTION 8.03. Other Remedies. In addition to the foregoing, the Authority shall also have the right:

(a) by mandamus or other action or proceeding or suit at law or in equity to enforce its rights against the City or any officer or employee thereof, and to compel the City or any such officer or employee to perform and carry out its or his or her duties under the law and the agreements and covenants required to be performed by it or him or her contained in this Installment Sale Agreement;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Authority; or

(c) by suit in equity upon the happening of an Event of Default to require the City and its officers and employees to account as the trustee of an express trust.

SECTION 8.04. Remedies Not Exclusive; No Waiver of Rights. No remedy herein conferred upon or reserved to the Authority or the Trustee is intended to be exclusive of any other available remedy or remedies, but each and every such remedy, to the extent permitted by law, shall be cumulative and shall be in addition to every other remedy given under this Installment Sale Agreement or now or hereafter existing at law or in equity or otherwise. In order to entitle the Authority or the Trustee to exercise any remedy, to the extent permitted by law, reserved to it or contained in this Installment Sale Agreement, it shall not be necessary to give any notice, other than such notice as may be herein expressly required. Such rights and remedies as are given to the Authority hereunder shall also extend to the Trustee, and the Trustee may exercise any rights under this Installment Sale Agreement, and the Trustee and the Owners of the Bonds issued under the Trust Agreement shall be deemed third party beneficiaries of all covenants and conditions herein contained.

No delay in exercising or omitting to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver of any such default or an acquiescence therein, and every such right and power may be exercised from time to time and as often as may be deemed expedient.

SECTION 8.05. Expenses on Default. In the event the City should default under any of the provisions of this Installment Sale Agreement and the Authority or the Trustee should employ attorneys or incur other expenses for the collection of the payments due hereunder, the City agrees that it will on demand therefor pay to the Authority or the Trustee the fee of such attorneys and such other expenses so incurred by the Authority or the Trustee.

SECTION 8.06. Notice of Default. The City agrees that, as soon as is practicable, and in any event within ten (10) days of the City's actual gaining knowledge thereof, the City will furnish the Trustee notice of any event which is an Event of Default pursuant to Section 8.01 hereof which has occurred and is continuing on the date of such notice, which notice shall set forth the nature of such event and the action which the City proposes to take with respect thereto.

ARTICLE IX

DISCHARGE OF OBLIGATIONS

SECTION 9.01. Escrow Deposit. Notwithstanding any other provision of this Installment Sale Agreement, the City may on any date secure the payment of Installment Payments, in whole or in part, by irrevocably depositing with the Trustee, an escrow agent, or any other fiduciary an amount of cash when, together with amounts on deposit in the Bond Fund and the accounts therein, is either (a) sufficient to pay all such Installment Payments, including the principal and interest components thereof, in accordance with the Installment Payment schedules set forth in Exhibit C, or (b) invested in whole or in part in Federal Securities in such amount as will, in the written opinion of an Independent Accountant, together with interest to accrue thereon and together with any cash which is so deposited, be fully sufficient to pay all such Installment Payments when due pursuant to Section 3.01 or when due on any optional prepayment date pursuant to Section 3.02, as the City shall instruct at the time of said deposit. At any time the City makes an escrow deposit with respect to all of the then outstanding Installment Payments pursuant to this Section, all obligations of the City under this Installment Sale Agreement, and all security provided by this Installment Sale Agreement for said obligations, shall cease and terminate, except as provided in Section 9.03 below. Said escrow deposit shall be deemed to be and shall constitute a special fund for the payment of Installment Payments in accordance with the provisions of this Installment Sale Agreement.

SECTION 9.02. Credit for Amounts on Deposit. In the event of prepayment of the principal components of the Installment Payments in full under this Article IX, such that the Trust Agreement shall be discharged by its terms as a result of such prepayment, and upon payment in full of all Additional Payments and other amounts then due and payable hereunder, all available amounts then on deposit in the funds and accounts established under the Trust Agreement shall be credited towards the amounts then required to be so prepaid.

SECTION 9.03. Effect of Prepayment. In the event that the City prepays all remaining Installment Payments in full pursuant to this Article IX, the City's obligations under this Installment Sale Agreement shall thereupon cease and terminate, including but not limited to the City's obligation to pay Installment Payments under Section 3.01; provided, however, that

the City's obligations to compensate and indemnify the Trustee pursuant to Sections 3.03 and 7.03 shall survive such prepayment.

ARTICLE X

BOND INSURANCE POLICY

[to come]

ARTICLE XI MISCELLANEOUS

SECTION 11.01. City's Right to Institute Actions. Nothing contained in this Installment Sale Agreement shall be construed to release the Authority or the Trustee from the performance of any of the agreements on its part contained herein or in the Trust Agreement, and in the event the Authority or the Trustee shall fail to perform any such agreements, the City may institute such action against the Authority or the Trustee as the City may deem necessary to compel performance so long as such action does not abrogate the obligations of the City contained in the preceding paragraph. The City may, however, at the City's own cost and expense and in the City's own name or in the name of the Authority prosecute or defend any action or proceeding or take any other action involving third persons which the City deems reasonably necessary in order to secure or protect the City's rights hereunder, and in such event the Authority hereby agrees to cooperate fully with the City and to take such action necessary to effect the substitution of the City for the Authority in such action or proceeding if the City shall so request.

SECTION 11.02. Notices; Business Days. All notices hereunder shall be governed by the provisions set forth in Section 13.05 of the Trust Agreement. Any action required to occur hereunder on a day which is not a Business Day shall be required to occur on the next succeeding Business Day with the same effect as if made on such non-Business Day

SECTION 11.03. Content of Statements and Opinions. Every statement or opinion provided for in this Installment Sale Agreement with respect to compliance with any provision hereof shall include (a) a statement that the person making or giving such statement or opinion has read such provision and the definitions herein relating thereto; (b) a brief statement as to the nature and scope of the examination or investigation upon which the statement or opinion is based; (c) a statement (i) that, in the opinion of such person, he has made or caused to be made such examination or investigation as is necessary to enable him to express an informed opinion with respect to the subject matter or (ii) that he has made or caused to be made his examination or investigation with respect to the subject matter in accordance with specified professional standards; and (d) a statement as to whether, in the opinion of such person, such provision has been complied with.

Any such statement or opinion made or given by an officer of the Authority or the City may be based, insofar as it relates to legal, accounting or City matters, upon a statement or

opinion of or representation by Counsel or an Accountant, unless such officer knows, or in the exercise of reasonable care should have known, that the statement, opinion or representation with respect to the matters upon which such statement or statements may be based, as aforesaid, is erroneous. Any such statement or opinion made or given by Counsel or an Accountant may be based, insofar as it relates to factual matters (with respect to which information is in the possession of the Authority or the City, as the case may be) upon a statement or opinion of or representation by an officer of the Authority or the City, unless such Counsel or Accountant knows, or in the exercise of reasonable care should have known, that the statement or opinion or representation with respect to the matters upon which such person's statement or opinion or representation may be based, as aforesaid, is erroneous. The same officer of the Authority or the City, or the same Counsel or Accountant, as the case may be, need not certify to all of the matters required to be certified under any provision of this Installment Sale Agreement, but different officers, Counsel or Accountants may certify to different matters, respectively.

SECTION 11.04. Governing Law. This Installment Sale Agreement shall be construed in accordance with and governed by the Constitution and laws of the State.

SECTION 11.05. Severability of Invalid Provisions. If any one or more of the provisions contained in this Installment Sale Agreement shall for any reason be held to be invalid, illegal or unenforceable in any respect, then such provision or provisions shall be deemed severable from the remaining provisions contained in this Installment Sale Agreement and such invalidity, illegality or unenforceability shall not affect any other provision of this Installment Sale Agreement, and this Installment Sale Agreement shall be construed as if such invalid or illegal or unenforceable provision had never been contained herein. The Authority and the City each hereby declares that it would have entered into this Installment Sale Agreement and each and every other Section, paragraph, sentence, clause or phrase hereof irrespective of the fact that any one or more Sections, paragraphs, sentences, clauses or phrases of this Installment Sale Agreement may be held illegal, invalid or unenforceable.

SECTION 11.06. Binding Effect. This Installment Sale Agreement shall inure to the benefit of and shall be binding upon the Authority, the City, the Trustee and their respective successors and assigns, subject, however, to the limitations contained herein.

SECTION 11.07. Further Assurances. The City and the Authority each agrees that it will execute and deliver any and all such further agreements, instruments, financing statements or other assurances as may be reasonably necessary or requested by the other party or the Trustee to carry out the intention or to facilitate the performance of this Installment Sale Agreement, including, without limitation, to perfect and continue the security interests herein intended to be created.

SECTION 11.08. Amendments. This Installment Sale Agreement may not be effectively amended, changed, modified, altered or terminated except by the written agreement of the City and the Authority entered into in compliance with Section 7.06 of the Trust Agreement.

SECTION 11.09. Disclaimer of Warranties. The Authority makes no warranty or representation, either express or implied, as to the value, design, condition, merchantability or

fitness for any particular purpose or fitness for the use contemplated by the City of the Facilities or the 2004 Projects, or any portion thereof, or any other representation or warranty with thereto. In no event shall the Authority be liable for incidental, indirect, special or consequential damages, in connection with this Installment Sale Agreement or the existence, furnishing or functioning of the Facilities or the 2004 Projects, or the City's or the Authority's or any other person's use thereof, except such damages as may arise by reason of the Authority's breach of this Installment Sale Agreement.

SECTION 11.10 Waiver of Personal Liability. No member, director, officer, agent or employee of the Authority or director, officer, agent or employee of the City shall be individually or personally liable for the payment of Installment Payments or any other sum hereunder or be subject to any personal liability or accountability by reason of the execution and delivery of this Installment Sale Agreement; provided, however, nothing herein contained shall relieve any such member, director, officer, agent or employee from the performance of any official duty provided by law or by this Installment Sale Agreement.

SECTION 11.11 Execution of Counterparts. This Installment Sale Agreement may be executed in any number of counterparts, each of which shall for all purposes be deemed to be original and all of which shall together constitute but one and the same instrument.

[Remainder of Page Intentionally Left Blank]

IN WITNESS WHEREOF, the Authority and the City have caused this Installment Sale Agreement to be executed in their respective names by their duly authorized representatives, all as of the date first above written.

CITY OF MORGAN HILL

By _____
City Manager

MORGAN HILL FINANCING AUTHORITY

By _____
Chief Administrative Officer

EXHIBIT A

DESCRIPTION OF FACILITIES

1. All of the 2004 Projects as described in Exhibit B.
2. The City shall have the right from time to time in its sole discretion to amend the description of the Facilities hereunder. In order to exercise such right, the City shall file with the Authority and the Trustee an amended Exhibit A.

EXHIBIT B

DESCRIPTION OF 2004 PROJECTS

- 1.
2. The 2004 Projects may also include any other capital addition to or replacement of any portion of the Water System as to which the City has received an opinion of Bond Counsel to the effect that the payment of the costs of such capital addition or replacement with moneys in the Project Fund will not, in and of itself, adversely affect the Tax-exempt status of Bonds issued and Outstanding under the Trust Agreement.

EXHIBIT C
SCHEDULE OF INSTALLMENT PAYMENTS

<u>Date</u>	<u>Principal Component</u>	<u>Interest Component</u>	<u>Total Installment Payment</u>
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OFFICIAL NOTICE INVITING BIDS
\$ _____
MORGAN HILL FINANCING AUTHORITY
WATER REVENUE BONDS
SERIES 2004

NOTICE IS HEREBY GIVEN that faxed or electronic bids for the purchase of \$ _____* principal amount of Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 (the "Series 2004 Bonds") will be received by the Morgan Hill Financing Authority (the "Authority") at the place, in the manner and, subject to postponement (as described herein under the caption "TERMS OF SALE – Postponement"), at the time and date specified below:

Date and Time: **9:00 A.M. California Time on Tuesday, _____, 2004**, and so long as a proposal has not theretofore been accepted by the Authority, on any date thereafter without further advertising.

Electronic Bids Bid proposals may be submitted electronically through PARITY® ("Parity"), as provided below.

Faxed Bids: Bid proposals may also be submitted by facsimile; however, none of the Authority, the City of Morgan Hill (the "City"), RBC Dain Rauscher Inc., Financial Advisor to the Authority, nor Richards, Watson & Gershon, A Professional Corporation, Bond Counsel, takes any responsibility for any difficulties in transmitting bids prior to the 9:00 A.M. deadline. The number to be used to transmit telecopied bids is (415) 445-8679.

See "TERMS OF SALE – Warnings Regarding Faxed Bids" and "– Warnings Regarding Electronic Bids" herein.

SEAL BIDS WILL NOT BE ACCEPTED.

Terms of Bonds; Preliminary Official Statement: The terms of issuance, principal, and interest payment, redemption, security, tax exemption and all other information regarding the Series 2004 Bonds and the Authority are given in the Preliminary Official Statement for the Series 2004 Bonds, dated _____, 2004 (the "Preliminary Official Statement"), which each bidder must have obtained and reviewed prior to bidding for the Series 2004 Bonds. This Official Notice Inviting Bids contains certain information for quick reference only, is not a summary of the issue and governs only the terms of the sale of, bidding for and closing procedures with respect to the Series 2004 Bonds. Bidders must read the entire Preliminary Official Statement to obtain information essential to the making of an informed investment decision. Capitalized terms used herein and not defined herein shall have the meanings set forth in the Preliminary Official Statement. The Series 2004 Bonds will be issued pursuant to a Trust Agreement, dated as of October 1, 2004 (the "Trust Agreement"), by and between the Authority and BNY Western Trust Company, as trustee (the "Trustee").

Opening of Bids: The bids will be received on the date, at the time and place on the dates shown above and will be presented to a duly authorized officer of the Authority who will, on behalf of the Authority, determine and accept the conforming bid with the lowest true interest cost as the best bid for the Series 2004 Bonds, subject to the Authority's right to reject any and all bids as set forth below.

Book-Entry Only: The Series 2004 Bonds will be issued in book-entry form only, initially registered in the name of CEDE & CO., as nominee of The Depository Trust Company, New York, New York ("DTC"). Individual purchases will be made in the maturities described below under the caption "TERMS OF BONDS – Maturities." Payments of principal and interest to DTC shall be the responsibility of the Trustee and disbursement of such payments to the beneficial owners shall be the responsibility of DTC's direct-participants or indirect participants. The fees and charges of DTC shall be borne by the prevailing bidder.

TERMS OF BONDS

Issue; Security: The Series 2004 Bonds are issuable in the aggregate principal amount of \$_____ consisting of fully registered bonds in denominations of \$5,000 or any integral multiple thereof not exceeding the principal amount of the Series 2004 Bonds maturing at any one time, all dated as of their date of delivery (currently expected to be _____, 2004), and comprising all of the Series 2004 Bonds authorized. The Series 2004 Bonds will be issued pursuant to, and are more particularly described in, the Trust Agreement. The Series 2004 Bonds are primarily payable from Revenues, consisting of certain installment payments (the "Installment Payments") to be made by the City to the Authority pursuant to a Installment Sale Agreement, dated as of October 1, 2004 (the "Installment Sale Agreement"), by and between the Authority and the City. The Installment Payments are special limited obligations of the City payable solely from and secured by a pledge of Net Revenues (defined in the Installment Sale Agreement) of the City's water system (the "Water System"). The City's obligation to pay the Installment Payments out of the revenues of the Water System is ranked on a parity with the loan (the "2003 Loan") made by the Authority to the City pursuant to a Loan Agreement, dated as of December 1, 2003, and is subordinate to the City's obligation with respect to installment payments relating to the outstanding Refunding Certificates of Participation (Water System Improvement Projects) Series 1999 (the "1999 Certificates"). As of September 30, 2004, the remaining outstanding principal amount of the 2003 Loan is \$1,470,437 and the remaining outstanding principal amount of the outstanding principal amount of the 1999 Certificate is \$4,360,000

Copies of the Trust Agreement and the Installment Sale Agreement will be furnished to any interested bidder upon request.

Authority; Purpose: The governing board of the Authority adopted Resolution No. MHFA-__ on October 6, 2004, authorizing the issuance of the Series 2004 Bonds in an aggregate principal amount not to exceed \$8,000,000. The Series 2004 Bonds are to be issued by the Authority under and pursuant to the Marks-Roos Local Bond Pooling Act of 1985 (Article 4 of Chapter 5 of Division 7 of Title 1 of the California Government Code) to (i) provide funds to the City to finance certain capital improvements for the Water System, (ii) to fund a reserve account for the Series 2004 Bonds, and (iii) pay costs of issuance of the Series 2004 Bonds.

Maturities: The Series 2004 Bonds will mature or be subject to mandatory sinking account redemption on June 1 in each of the years 20__ to 20__ inclusive, as set forth below. Each bidder may specify in its bid whether, for any particular year, the Series 2004 Bonds will be term bonds subject to mandatory sinking account redemption in the applicable principal amount set forth in the bid form. Interest on the Series 2004 Bonds will be payable on each June 1 and December 1, commencing June 1, 2005. Other criteria for setting the maturity amounts of the Series 2004 Bonds are described under the "TERMS OF SALE" below.

Maturity Date
(June 1)

Principal
Amount*

Maturity Date
(June 1)

Principal
Amount*

[to come]

Adjustment of Principal Amount of Any Maturity: The Authority reserves the right to increase or decrease the principal amount of any maturity of the Series 2004 Bonds, as the Authority deems advisable in order to accomplish its financing objectives. Notice of such increase or decrease shall be given by the Authority to the successful bidder as soon as practicable following the notification of award. Any such adjustment will change the total (but not the average per Series 2004 Bond) dollar amount of the underwriter's discount and original issue discount or premium, if any, provided in such bid. No such adjustment will have the effect of altering the basis upon which the best bid is determined or shall change the aggregate principal amount of the Series 2004 Bonds to be issued by more than 10 percent.

Delivery and Payment: The Series 2004 Bonds will be issued in book-entry-only form registered in the name of Cede & Co. (DTC's partnership nominee). Prior to the day of closing, which is currently estimated to be on _____, 2004, the Series 2004 Bonds, in the form of a single typewritten certificate for each maturity of Series 2004 Bonds, will be delivered to DTC. Payment for the Series 2004 Bonds must be made by wire transfer to the Trustee for the benefit of the Authority in immediately available funds. Any expense of providing immediately available funds, whether by transfer of Federal Reserve Bank funds or otherwise, shall be borne by the winning bidder. Upon closing, the Trustee shall notify DTC of receipt of payment by the purchaser, at which time DTC (in accordance with the Letter of Representations defined below) will credit the account of the successful bidder and process the book-entry deliveries to the accounts of the subsequent purchasers of interests in the Series 2004 Bonds. On each June 1 and December 1, commencing June 1, 2005, the Trustee shall remit to DTC funds to pay all outstanding principal and interest due with respect to the Series 2004 Bonds.

To induce DTC to accept the Series 2004 Bonds as eligible for the book-entry-only form of issuance, the Authority has heretofore executed a Letter of Representations with DTC setting forth the terms and conditions of, and procedures for, the book-entry-only form of issuance. The successful bidder shall complete and provide to DTC's Underwriting Department the Eligibility Questionnaire in the form required by DTC not later than five (5) business days prior to closing.

Redemption from Optional Prepayments of Base Rental: The Series 2004 Bonds maturing on or before June 1, 2014 are not subject to optional redemption prior to their respective maturity dates. The Series 2004 Bonds maturing on or after June 1, 2015 will be subject to redemption prior to their respective maturity dates, as a whole or in part, on any date on or after June 1, 2014, from prepayments of Installment Payments made at the option of the City pursuant to the Installment Sale Agreement, at a redemption price equal to 100 percent of the principal amount of the Series 2004 Bonds to be redeemed, plus accrued interest thereon to the date of redemption, without premium.

* Preliminary; subject to change.

Extraordinary Redemption: The Series 2004 Bonds are subject to mandatory redemption, as a whole from prepaid Installment Payments made by the City from a condemnation award or from insurance proceeds at the principal amount thereof and accrued interest thereon to the date fixed for redemption, without premium.

Sinking Account Redemption; Purchase in Lieu of Redemption: *Any bidder may, at its option, specify that one or more maturities of the Series 2004 Bonds will consist of term bonds which are subject to mandatory sinking account redemption in consecutive years immediately preceding the maturity thereof, as designated in the bid of such bidder.* In the event that the bid of the successful bidder specifies that any maturity of Series 2004 Bonds will be term bonds, such term bonds will be subject to mandatory sinking account redemption on June 1 in each year so designated in the bid, in the respective amounts for such years as set forth above under the subheading "Maturities," at a redemption price equal to the principal amount thereof to be redeemed together with accrued interest thereon to the redemption date, without premium.

Selection of Bonds for Redemption: Whenever less than all of the outstanding Series 2004 Bonds maturing on any one date are called for redemption, the Trustee shall select the Series 2004 Bonds to be redeemed from the outstanding Series 2004 Bonds or such given portion thereof not previously called for redemption, among maturities (unless the maturity or maturities are otherwise specified in the Trust Agreement or in writing by the Authority) and by lot within a maturity in any manner which the Trustee in its discretion shall deem appropriate.

TERMS OF SALE

Interest Rate For the Series 2004 Bonds; Purchase Price: The rate or rates bid, as the case may be, may not exceed five and three-quarters percent (5.75%) per annum for the Series 2004 Bonds, payable commencing June 1, 2005, and semiannually thereafter on June 1 and December 1 of each year. Each rate bid must be a multiple of one-eighth of one percent (1/8 %) or one-twentieth of one percent (1/20 %). All Series 2004 Bonds of the same maturity must carry the same interest rate. No Series 2004 Bond may bear more than one interest rate, and each Series 2004 Bond must bear interest at the rate specified in the bid from its date to its fixed maturity date. **The purchase price bid for the Series 2004 Bonds shall not be less than ___ percent of the principal amount thereof.** Each bid must be in accordance with all other terms and conditions set forth in this notice. See "TERMS OF SALE – Official Statement and Other Information."

Sinking Account Redemption: Any bidder may, at its option, specify that one or more maturities of Series 2004 Bonds will consist of term bonds which are subject to mandatory sinking account redemption in consecutive years immediately preceding the maturity thereof, as designated in the bid of such bidder. In the event that the bid of the successful bidder specifies that any maturity of Series 2004 Bonds will be a term bond, such term bond will be subject to mandatory sinking account redemption on July 15 in each applicable year in the principal amount for such year as set forth above under the heading "TERMS OF BONDS – Maturities," at a redemption price equal to the principal amount thereof to be redeemed together with accrued interest thereon to the redemption date, without premium.

Electronic Bids: Electronic bids must conform to the procedures established by Parity. Solely as an accommodation to bidders, electronic bids will be received exclusively through Parity in accordance with this Official Notice Inviting Bids until 9:00 a.m., California time, but no bid will be received after the time specified for receiving bids. To the extent any instructions or directions set forth in Parity conflict with this Official Notice of Inviting Bids, the terms of this Official Notice of Inviting Bids shall

control. For further information about Parity, potential bidders may contact Parity at 40 West 23rd Street, 5th Floor, New York, New York 10010; Telephone: (212) 404-8102.

THE AUTHORITY RETAINS ABSOLUTE DISCRETION TO DETERMINE WHETHER ANY BID, WHETHER FAXED OR ELECTRONIC, IS TIMELY, LEGIBLE AND COMPLETE. THE AUTHORITY TAKES NO RESPONSIBILITY FOR INFORMING ANY BIDDER PRIOR TO THE TIME FOR RECEIVING BIDS THAT ITS BID IS INCOMPLETE, ILLEGIBLE OR NOT RECEIVED.

Warnings Regarding Facsimile Bids: THE RECEIVING FAX MACHINE WILL BE DISCONNECTED AT THE DEADLINE FOR RECEIPT OF BIDS. ANY BIDS PRINTED THEREAFTER BY THE RECEIVING FAX MACHINE, PROVIDED THAT THE INTEREST RATES, TOTAL PURCHASE PRICE AND NAME AND SIGNATURE OF THE BIDDER ARE CLEARLY LEGIBLE, WILL BE CONSIDERED TIMELY; HOWEVER, NEITHER THE CITY, THE AUTHORITY, THE FINANCIAL ADVISOR, NOR BOND COUNSEL SHALL BE RESPONSIBLE FOR, AND THE BIDDER EXPRESSLY ASSUMES THE RISK OF, ANY INCOMPLETE, ILLEGIBLE OR UNTIMELY BID SUBMITTED BY SUCH BIDDER BY FACSIMILE TRANSMISSION, INCLUDING, WITHOUT LIMITATION, BY REASON OF GARBLED TRANSMISSION, MECHANICAL FAILURE, ENGAGED TELEPHONE OR TELECOMMUNICATIONS LINES AT THE PLACE OF BID OPENING.

Warning Regarding Electronic Bids: THE AUTHORITY WILL ACCEPT BIDS IN ELECTRONIC FORM SOLELY THROUGH PARITY ON THE OFFICIAL BID FORM CREATED FOR SUCH PURPOSE. EACH BIDDER SUBMITTING AN ELECTRONIC BID UNDERSTANDS AND AGREES BY DOING SO THAT IT IS SOLELY RESPONSIBLE FOR ALL ARRANGEMENTS WITH PARITY, THAT THE AUTHORITY NEITHER ENDORSES NOR EXPLICITLY ENCOURAGES THE USE OF PARITY, AND THAT PARITY IS NOT ACTING AS AN AGENT OF THE AUTHORITY. INSTRUCTIONS AND FORMS FOR SUBMITTING ELECTRONIC BIDS MUST BE OBTAINED FROM PARITY, AND THE AUTHORITY ASSUMES NO RESPONSIBILITY FOR ENSURING OR VERIFYING BIDDER COMPLIANCE WITH THE PROCEDURES OF PARITY. THE AUTHORITY SHALL ASSUME THAT ANY BID RECEIVED THROUGH PARITY HAS BEEN MADE BY A DULY AUTHORIZED AGENT OF THE BIDDER.

THE AUTHORITY WILL MAKE ITS BEST EFFORTS TO ACCOMMODATE ELECTRONIC BIDS; HOWEVER THE AUTHORITY, THE FINANCIAL ADVISOR AND BOND COUNSEL ASSUME NO RESPONSIBILITY FOR ANY ERROR CONTAINED IN ANY BID SUBMITTED ELECTRONICALLY OR FOR FAILURE OF ANY BID TO BE TRANSMITTED, RECEIVED OR OPENED AT THE OFFICIAL TIME FOR RECEIPT OF BIDS. THE OFFICIAL TIME FOR RECEIPT OF BIDS WILL BE DETERMINED BY THE AUTHORITY AT THE PLACE OF BID OPENING, AND THE AUTHORITY SHALL NOT BE REQUIRED TO ACCEPT THE TIME KEPT BY PARITY AS THE OFFICIAL TIME.

IN THE EVENT OF A MALFUNCTION IN THE ELECTRONIC BIDDING PROCESS, BIDDERS SHOULD SUBMIT THEIR BIDS ON THE OFFICIAL BID FORM ATTACHED HERETO BY FACSIMILE TO: (415) 445-8679.

Award of Bonds: The Series 2004 Bonds will be awarded by the Authority to the lowest responsible bidder therefor, considering the rate or rates specified and the discount bid or premium offered, if any. The lowest bidder for the Series 2004 Bonds shall be the bidder submitting the price resulting in the lowest true interest cost. The true interest cost will be the nominal interest rate which, when computed semiannually and used to discount the total debt service payments on the Series 2004 Bonds to the dated date of the Series 2004 Bonds, results in an amount equal to the price bid for the

Series 2004 Bonds (assuming that any term bonds are redeemed as scheduled pursuant to mandatory sinking account payments) at the interest rate or rates specified in the bid. In the event that two or more bidders have bid the same interest cost, the award shall be made by lot, subject to the other provisions of this notice.

Right of Rejection: The Authority reserves the right, in its discretion, to reject any and all bids and, to the extent permitted by law, to waive any irregularity, non-conformity or informality in any bid.

Prompt Award: The Authority will take action awarding the Series 2004 Bonds or rejecting all bids for Series 2004 Bonds not later than 26 hours after the time herein prescribed for the receipt of bids, unless such time is waived by the successful bidder. Notice of the award will be given promptly to the successful bidder.

Form of Bid for the Series 2004 Bonds: Each bid for the Series 2004 Bonds must be delivered via Parity or faxed to the number set forth above. Each bid must be unconditional and in accordance with the terms and conditions set forth herein, or permitted herein, and, in the case of faxed bids, must be submitted on, or in substantial conformance with, bid forms provided by the Authority.

Deposit: A Good Faith Deposit ("Deposit") in the form of a certified or cashier's check or a Financial Surety Bond in the amount of \$_____, payable to the order of the Authority, is required for each bid to be considered. If a check is used, it must be payable on the date of the bid opening in same day or next day funds and must be delivered to the Authority, care of the City of Morgan Hill, 17555 Peak Avenue, Morgan Hill, CA 95037, Attention: Director of Finance, prior to the time bids are received, and will be returned if such bid is not the winning bid. If a Financial Surety Bond is used, it must be from an insurance company licensed to issue such a bond in the State of California, and such bond must be submitted to the Authority or its Financial Advisor prior to the opening of the bids. The Financial Surety Bond must identify each bidder whose Deposit is guaranteed by such Financial Surety Bond. If the Series 2004 Bonds are awarded to a bidder utilizing a Financial Surety Bond, then that winning bidder ("Purchaser") is required to wire transfer such amount as instructed by the Authority or its Financial Advisor not later than 3:30 P.M., New York time, on the next business day following the award. If such Deposit is not received by that time, the Financial Surety Bond may be drawn by the Authority to satisfy the Deposit requirement. No interest on the Deposit will accrue to the Purchaser. The Deposit will be applied to the purchase price of the Series 2004 Bonds. The Deposit accompanying any accepted bid shall be cashed and the proceeds thereof applied to the purchase price. In the event the successful bidder fails to honor its accepted bid, the Deposit will be retained by the Authority as and for full liquidated damages.

List of Members of Account: Bidders are requested to list on the bid form the names of the members of the account on whose behalf the bid is made. The successful bidder will be required to submit a list of all syndicate members in addition to the managers not later than 24 hours after receiving a verbal award.

CUSIP: It is anticipated that CUSIP numbers will be printed on the Series 2004 Bonds, but neither the failure to print such numbers on any Series 2004 Bond nor any error with respect thereto shall constitute cause for a failure or refusal by the purchaser thereof to accept delivery of and pay for the Series 2004 Bonds in accordance with the terms hereof. The cost of the assignment of CUSIP numbers shall be paid by the Purchaser. It will be the Purchaser's responsibility to obtain CUSIP numbers and provide them to Bond Counsel and the Trustee.

Delivery; Form of Bonds: Delivery is expected to be made on or about _____, 2004, or such other date as may be agreed upon by the City and the Purchaser. The Series 2004 Bonds will be

issued by means of a book-entry system with no physical distribution of bond certificates made to the public. One bond certificate for each maturity of the Series 2004 Bonds will be issued to DTC, and immobilized in its custody. The book-entry system will evidence ownership of the Series 2004 Bonds in the principal amount of five thousand dollars (\$5,000) or any multiple thereof, with transfers of ownership effected on the records of DTC and its participants. The Purchaser, as a condition to the delivery of their Series 2004 Bonds, shall be required to deposit the bond certificates with DTC, registered in the name of Cede & Co., its nominee.

Place of Delivery; Form of Payment: Delivery of the Series 2004 Bonds to the Purchaser will be made at DTC offices upon payment therefor in Federal Reserve Funds (immediately available) or at any other place agreeable to both the Authority and the Purchaser.

California Debt and Investment Advisory Commission Fee: All bidders are advised that it will be the responsibility of the Purchaser to pay the statutory fee to the California Debt and Investment Advisory Commission.

Bond Insurance: _____ has provided the City with its commitment to issue a financial guaranty insurance policy (the "Bond Insurance Policy") insuring, when due, payment of principal and interest on the Series 2004 Bonds. The City will be responsible for payment of the cost of the premiums for the Bond Insurance Policy.

Ratings: Moody's Investors Service ("Moody's) and Standard & Poor's ("S&P") are expected to assign ratings of "Aaa" and "AAA," respectively, to the Series 2004 Bonds, conditioned on the issuance by the Bond Insurer of the Bond Insurance Policy at the time of delivery of the Series 2004 Bonds. Such ratings reflect only the views of such organizations and any desired explanation of the significance of such ratings may be obtained from Moody's and S&P. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by the rating agencies, if in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Series 2004 Bonds.

Certification: The Authority will deliver to the Purchaser one or more certificate(s) of an officer of the Authority and an officer of the City, dated the date of delivery of the Series 2004 Bonds, stating that, as of the date thereof, to the best knowledge of such officer: (i) that the Official Statement does not contain an untrue statement of a material fact or omit to state any material fact necessary, in order to make the statements made therein, in light of the circumstances under which they were made, not misleading, (ii) that such officer knows of no material adverse change in the condition of the Authority (or the City, as applicable) which would make it unreasonable for the purchaser of the Series 2004 Bonds to rely upon the Official Statement in connection with the resale of the Series 2004 Bonds, and (iii) that there is no litigation pending and which has been served upon the Authority (or the City, as applicable), or threatened against the Authority (or the City, as applicable), to restrain or enjoin the execution or delivery of the Series 2004 Bonds, the Trust Agreement or the Installment Sale Agreement, or in any way questioning or affecting the validity of the foregoing or any of the proceedings for the authorization, sale, execution or delivery of the Series 2004 Bonds.

Continuing Disclosure: The City will covenant for the benefit of owners of the Series 2004 Bonds to cause certain financial information and operating data relating to the City to be provided in order to assist the purchaser in complying with Securities Exchange Commission Rule 15c2-12(b)(5). The specific nature of the financial information, operating data and material events to be disclosed on an ongoing basis is summarized in the Preliminary Official Statement.

Official Statement and Other Information: Copies of the Trust Agreement, the Installment Sale Agreement, this Official Notice Inviting Bids, the Bid Forms and Preliminary Official Statement will be furnished to any potential bidder upon request made to the Authority's Financial Advisor at: RBC Dain Rauscher, at 345 California Street, Suite 2800, San Francisco, CA 94104, telephone: (415) 445-8676, e-mail: richard.morales@rbcdain.com.

The Preliminary Official Statement is in a form deemed final by the Authority within the meaning of Rule 15c2-12(b)(1) (the "Rule") promulgated by the Securities and Exchange Commission except for the omission of certain information permitted to be omitted therefrom pursuant to the Rule, but is subject to revision, amendment and completion in a final Official Statement.

The Preliminary Official Statement is available on the Internet at www.i-dealprospectus.com. Bidders will be required to confirm their consent to delivery of the Preliminary Official Statement in electronic form and their review of a complete copy of the Preliminary Official Statement, as a condition to the acceptance of their bid by the City. The Internet posting of the Preliminary Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of, the securities described in the Preliminary Official Statement, in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction. To obtain printed copies of the Preliminary Official Statement please contact the party set forth in the first paragraph of this section.

Upon the sale of the Series 2004 Bonds, the Authority will publish the Official Statement in substantially the same form as the Preliminary Official Statement subject to minor additions, deletions, and revisions as required to complete the Preliminary Official Statement. Promptly after the sale date for the Series 2004 Bonds, but in no event later than seven (7) business days after the sale date of the Series 2004 Bonds, the Authority will provide the Purchaser with a reasonable number of copies of the Official Statement. Such final Official Statement may be obtained, without cost to the Purchaser, in an amount not greater than ___ to be mailed to a maximum of two addresses. The Purchaser agrees to supply the Authority all pricing information necessary to complete the Official Statement within 24 hours after the award of the Series 2004 Bonds. Additional copies of the final Official Statement may be obtained at additional cost.

By making a bid for the Series 2004 Bonds, the Purchaser agrees to (1) disseminate to all members of the underwriting syndicate copies of the final Official Statement, including any supplements prepared by the Authority, (2) promptly file a copy of the final Official Statement, including any supplements prepared by the Authority, with a Nationally Recognized Municipal Securities Information Repository, and (3) take any and all other actions necessary to comply with applicable Securities and Exchange Commission rules and Municipal Securities Rulemaking Board rules governing the offerings sale and delivery of the Series 2004 Bonds and the Official Statement to ultimate purchasers.

Prospective bidders should review the form of opinion of Bond Counsel set forth in Appendix D to the Preliminary Official Statement.

Tax-Exempt Status: In the opinion of Richards, Watson & Gershon, A Professional Corporation, Los Angeles, California, Bond Counsel, based on existing law and assuming compliance with certain covenants set forth in the documents pertaining to the Series 2004 Bonds and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), interest on the Series 2004 Bonds is not includable in gross income of the owners thereof for federal income tax purposes, and is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the Series 2004 Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's

alternative minimum tax and environmental tax liabilities. In the further opinion of Bond Counsel, interest on the Series 2004 Bonds is exempt from personal income taxes imposed by the State of California. Bond Counsel will express no other opinion as to any federal or state tax consequences of the ownership or disposition of the Series 2004 Bonds.

In the event that prior to the delivery of the Series 2004 Bonds (a) the interest on other obligations of the same type and character shall be declared to be taxable (either at the time of such declaration or at any future date) under any federal income tax laws, either by the terms of such laws or by ruling of a federal income tax authority or official which is followed by the Internal Revenue Service, or by decision of any federal court, or (b) any federal income tax law is adopted which will have a substantial adverse effect upon owners of the Series 2004 Bonds as such, the successful bidder for the Series 2004 Bonds may, at its options prior to the tender of the Series 2004 Bonds, be relieved of its obligation under the contract to purchase the Series 2004 Bonds.

Qualification for Sale; Blue Sky: Compliance with blue sky laws shall be the sole responsibility of the Purchaser. The Authority will furnish such information and take such action not inconsistent with law as the Purchaser may request and the Authority shall deem necessary or appropriate to qualify the Series 2004 Bonds for offer and sale under the blue sky or other securities laws and regulations of such states and other jurisdictions of the United States of America as may be designated by the Purchaser; provided, however, that the Authority shall not execute a general or special consent to service of process or qualify to do business in connection with such qualification or determination in any jurisdiction. The Purchaser will not offer to sell or solicit any offer to buy the Series 2004 Bonds in any jurisdiction where it is unlawful for such Purchaser to make such offer, solicitation or sale, and the Purchaser shall comply with the blue sky and other securities laws and regulations of the states and jurisdictions in which the Purchaser sells the Series 2004 Bonds.

Reoffering Price: The Purchaser will, within one hour after being notified of the award of the Series 2004 Bonds, advise the Financial Advisor of the initial public offering prices of the Series 2004 Bonds. The Purchaser will also be required, prior to delivery of the Series 2004 Bonds, to furnish a certificate acceptable to Bond Counsel, stating that the amount of the initial offering price to the public (excluding bond houses and brokers) at which a substantial portion (at least 10 percent) of the Series 2004 Bonds of each maturity were sold and that there was a bona fide public offering made of each maturity of the Series 2004 Bonds.

Right to Modify or Amend: The Authority reserves the right to modify or amend this Official Notice Inviting Bids; however, such notifications of amendments shall be made not later than one business day prior to the bid opening and communicated through The Bond Buyer Wire (available at TM3, the Thompson Municipal Market Monitor at www.tm3.com).

Postponement: The Authority reserves the right to postpone, from time to time, the date established for the receipt of bids. Any such postponement will be announced through The Bond Buyer Wire not later than 1:00 P.M., New York time, on the last business day prior to any announced date for receipt of bids. If any date fixed for the receipt of bids and the sale of the Series 2004 Bonds is postponed, any alternative sale date will be announced through The Bond Buyer Wire at least 24 hours prior to such alternative sale date. On any such alternative sale date, bidders must submit a bid for the purchase of the Series 2004 Bonds in conformity in all respects with the provisions of this Official Notice Inviting Bids except for the date of sale and except for the changes announced through The Bond Buyer Wire.

DATED: _____, 2004

MORGAN HILL FINANCING AUTHORITY

By _____
Chief Administrative Officer

BID FORM
\$ _____
MORGAN HILL FINANCING AUTHORITY
WATER REVENUE BONDS
SERIES 2004

Dated: _____, 2004

To: Morgan Hill Financing Authority

Ladies and Gentlemen:

We offer to purchase all of the \$ _____ initial principal amount of Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 (the "Series 2004 Bonds"), more particularly described in your Official Notice Inviting Bids, dated as of _____, 2004, which is incorporated herein and made a part hereof, at a purchase price equal to the sum of (a) the principal amount thereof (b) [plus a premium of \$ _____] [less a discount of \$ _____], for an aggregate amount of \$ _____. This offer is for bonds bearing interest at the rates and in the form of serial or term bonds set forth on the second following page.

Unless otherwise designated in the space provided on the second following page, each maturity shall be a serial bond. The rates of interest for all mandatory sinking account payments (including payment at maturity) of a designated term bond must be identical and all identical rates will be deemed to be mandatory sinking account payments with respect to such term bond.

This bid is subject to acceptance no later than twenty-six (26) hours after the expiration of the time established for the final receipt of bids. We have noted the right reserved in the Official Notice Inviting Bids to adjust the size of the various maturities, as more fully described under "TERMS OF BONDS – Adjustment of Principal Amount of Any Maturity."

We have previously submitted to you, or there is enclosed herewith, a financial surety bond meeting the specifications set forth in the Official Notice Inviting Bids or a certified or cashier's check drawn on a responsible bank or trust company transacting business in the State of California payable on the date hereof in the same day or next day funds to the order of the Morgan Hill Financing Authority in the amount of \$ _____. If this proposal is not accepted, said good faith check is to be returned to us promptly after the award of the Series 2004 Bonds to the winning bidder.

We have noted that payment of the purchase price is to be made in immediately available Federal Reserve Funds by wire transfer at the time of delivery of the Series 2004 Bonds.

Our calculation of the true interest cost, which is considered informative only and not a part of the bid, is ____%.

We hereby request that _____ printed copies of the final Official Statement (a maximum of _____ copies to be mailed to no more than two addresses) be furnished at the expense of the Authority in accordance with the terms of the Official Notice Inviting Bids.

Subject to your acceptance hereof, we agree to make a bona fide public offering of all the Series 2004 Bonds at not in excess of the initial public offering prices (or less than the yields) set forth on the cover page of the Official Statement, plus accrued interest. We further agree to comply with the terms of the Official Notice Inviting Bids.

We represent that we have full and complete authority to submit this bid on behalf of our bidding syndicate and that the undersigned will serve as the lead manager for the group if the Series 2004 Bonds are awarded pursuant to this bid.

We certify (or declare) under penalty of perjury under the laws of the State of California that this proposal is genuine, and is not made in the interest of or on behalf of any person not named herein, and that the bidder has not directly or indirectly induced or solicited any other bidder or any other person, firm or corporation to refrain from bidding, and that the bidder has not in any manner sought by collusion to secure for itself an advantage over any other bidder.

Respectfully submitted,

Name of Firm

By:_____

By:_____

Address:_____

Telephone:_____

The following is a list of the members of our account on whose behalf this bid is made.

_____	_____
_____	_____
_____	_____

MATURITY SCHEDULE AND INTEREST RATES

[illegible]

* We acknowledge that the Authority may adjust the principal amount of any maturity of the Series 2004 Bonds in the manner described in the Official Notice Inviting Bids under the caption “TERMS OF BONDS – Adjustment of Principal Amount of Any Maturity.”

TRUST AGREEMENT

by and between the

MORGAN HILL FINANCING AUTHORITY

and

BNY WESTERN TRUST COMPANY

as Trustee

Dated as of October 1, 2004

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EXHIBIT A – Form of Series 2004 Bond

TRUST AGREEMENT

THIS TRUST AGREEMENT, dated as of October 1, 2004 (this "Trust Agreement"), is by and among the MORGAN HILL FINANCING AUTHORITY, a joint powers authority duly organized and existing under and by virtue of the laws of the State of California (the "Authority") and BNY WESTERN TRUST COMPANY, a banking corporation organized and existing under the laws of the State of California, as trustee (the "Trustee").

W I T N E S S E T H:

WHEREAS, the Authority is a joint powers authority duly organized and existing under and pursuant to Articles 1 through 4 (commencing with Section 6500) of Chapter 5 of Division 7 of Title 1 of the California Government Code (the "Act") and a Joint Exercise of Powers Agreement, dated as of November 5, 2003, by and between the City and the Morgan Hill Redevelopment Agency; and

WHEREAS, under the Act, the Authority is authorized to borrow money for the purpose of financing certain public capital improvements of the City, including facilities for the production, storage, transmission or treatment of water; and

WHEREAS, the City operates a water system (such system, including all additions, improvements and extensions thereto, the "Water System") to serve the City; and

WHEREAS, the Authority desires to assist the City with respect to the refinancing and financing of certain additions, improvements and extensions to the Water System; and

WHEREAS, for the purpose of providing funds to the City, the Authority has authorized the issuance of its Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 (the "Series 2004 Bonds") pursuant to the Trust Agreement, dated as of even date herewith, by and between the Authority and BNY Western Trust Company, as Trustee; and

WHEREAS, in furtherance of the above described financing, the City and the Authority have entered into an Installment Sale Agreement, dated as of even date herewith, pursuant to which the City has agreed to purchase the Facilities (as defined therein) from the Authority and make certain installment payments which have been calculated to be sufficient to enable the Authority to pay the principal of and interest and premium (if any) on the Series 2004 Bonds when due and payable; and

WHEREAS, all things necessary to cause the Series 2004 Bonds, when authenticated by the Trustee and issued as provided in this Trust Agreement, to be legal, special obligations of the Authority, enforceable in accordance with their terms, and to constitute this Trust Agreement a valid agreement for the uses and purposes herein set forth in accordance with its terms, have been done and taken, and the creation, execution and delivery of this Trust Agreement and the creation, execution and issuance of the Series 2004 Bonds, subject to the terms hereof, have in all respects been duly authorized;

NOW, THEREFORE, for and in consideration of the mutual covenants hereinafter contained, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

Section 1.01 Definitions. The terms defined in this Section 1.01 shall have the meanings ascribed to them in this Section 1.01 for all purposes of this Trust Agreement unless the context clearly indicates some other meaning. All capitalized terms used herein which are not defined herein but are defined in the Installment Sale Agreement shall have the meanings specified in the Installment Sale Agreement.

“Additional Bonds” means Bonds issued pursuant to Article VI.

“Additional Payments” means the payments so designated and required to be paid by the City pursuant to Section 3.03 of the Installment Sale Agreement.

“Annual Debt Service” means, with respect to the Bonds, for each Bond Year, the sum of (a) the interest falling due on all Outstanding Bonds in such Bond Year, assuming that all Outstanding Serial Bonds are retired as scheduled and that all Outstanding Term Bonds, if any, are redeemed from the Sinking Account, as may be scheduled (except to the extent that such interest is to be paid from the proceeds of sale of any Bonds), (b) the principal amount of the Outstanding Serial Bonds, if any, maturing by their terms in such Bond Year, and (c) the minimum amount of such Outstanding Term Bonds required to be paid or called and redeemed in such Bond Year.

“Annual Debt Service” shall not include (a) interest on Bonds which is to be paid from amounts constituting capitalized interest or (b) principal and interest allocable to that portion of the proceeds of any Bonds required to remain unexpended and to be held in escrow pursuant to the terms of a Supplemental Trust Agreement; provided that (i) projected interest earnings on such amounts, if any, deposited by the Authority in the Interest Account, are sufficient to pay the interest due on such portion of the Bonds so long as it is required to be held in escrow and (ii) the conditions for the release of such proceeds from escrow, insofar as they relate to Net Water Revenue coverage and satisfaction of the Reserve Requirement, are substantially the same as those for the issuance of Additional Bonds.

“Authority” means the Morgan Hill Financing Authority, a joint powers authority duly organized and existing under the laws of the State.

“Authorized Authority Representative” means the President, the Chief Administrative Officer or the Treasurer of the Authority (or any other person designated by any of them in writing) to act on behalf of the Authority.

“Authorized City Representative” means the Mayor, the City Manager, the Deputy City Manager or the Finance Director (or any person designated by any of them in writing) to act on behalf of the City.

“Average Annual Debt Service” means the average Annual Debt Service over all Bond Years.

“Beneficial Owners” means those individuals, partnerships, corporations or other entities for which the Direct Participants have caused DTC to hold Book-Entry Bonds.

“Bond” or “Bonds” means the Morgan Hill Financing Authority Water Revenue Bonds authorized by, and at any time Outstanding pursuant to, this Trust Agreement.

“Bond Counsel” means any attorney or firm of attorneys appointed by or acceptable to the Authority of nationally-recognized expertise in the issuance of obligations the interest on which is excludable from gross income for federal income tax purposes under the Code.

“Bond Fund” means the fund by that name established and held by the Trustee pursuant to Section 5.04.

“Bond Insurance Policy” means the municipal bond insurance policy, if any, issued by the applicable Bond Insurer and guaranteeing, in whole or in part, the payment of principal of and interest on a Series of Bonds.

“Bond Insurer” means the issuer or issuers of a policy or policies of municipal bond insurance (other than a Reserve Account Policy) obtained by the Authority to insure the payment of principal of and interest on a Series of Bonds issued under the Trust Agreement, when due otherwise than by acceleration, and which, in fact, are at any time insuring such Series of Bonds. With respect to the Series 2004 Bonds, the term “Bond Insurer” means _____. In the event that there are more than one Bond Insurer for the Bonds, the consent, approval or action of a Bond Insurer shall affect only the Bonds insured by such Bond Insurer; provided, however, with respect to Article XI hereof, the consent, approval or action required to be given or taken by the Bond Insurer shall be governed by the consent, approval or action of the Bond Insurer(s) insuring at least a majority of the aggregate amount of the Bonds then Outstanding.

“Bond Year” means each twelve-month period extending from June 2 in one calendar year to June 1 of the succeeding calendar year, both dates inclusive; except that the first Bond Year shall extend from the Closing Date to June 1, 2005.

“Book-Entry Bonds” mean the Bonds registered in the name of the nominee of DTC, or any successor securities depository for the Bonds, as the registered owner thereof, pursuant to the terms and provisions of Section 3.13.

“Business Day” means a day other than (i) a Saturday or Sunday or (ii) a day on which commercial banks in the city in which the Trustee maintains its Corporate Trust Office are

authorized or required by law or executive order to close, or (iii) a day on which the New York Stock Exchange is closed.

“City” means the City of Morgan Hill, California.

“Closing Date” means, with respect to each Series of Bonds, the date of original issuance of such Bonds. With respect to the Series 2004 Bonds, the Closing Date shall be _____, 2004.

“Code” means the Internal Revenue Code of 1986 as in effect on the date of original issuance of the Bonds or (except as otherwise referenced herein or in the Installment Sale Agreement) as it may be amended to apply to obligations issued on the date of original issuance of the Bonds, together with regulations promulgated, and official public guidance published, under the Code.

“Corporate Trust Office” means the principal corporate trust office of the Trustee in Los Angeles, California or such other offices as may be specified to the Authority by the Trustee in writing. With respect to presentation of Bonds for payment or for registration of transfer and exchange such term shall mean the office or agency of the Trustee at which, at any particular time, its corporate trust business shall be conducted.

“Costs of Issuance” means any costs or expenses paid or incurred in connection with the preparation, execution and delivery of the Bonds, including but not limited to fees and expenses of the Trustee and its counsel, printing costs, word processing costs, special counsel and other legal fees and expenses, rating agency fees, accounting fees, legal fees and other expenses incurred by the City or the Authority in connection with qualification or registration, or determining the exemption from registration or qualification, of the Bonds under the “Blue Sky” laws of any jurisdiction, fees payable to any other consultants or experts retained in connection with such preparation, execution and delivery, and any other cost, charge or fee in connection with the original issuance of the Bonds which constitutes a “cost of issuance” within the meaning of the Code.

“Costs of Issuance Fund” means the fund by that name established and held by the Trustee pursuant to Section 5.02.

“Counsel” means an attorney at law, or firm of attorneys, of recognized standing and who are qualified to pass on the legality of the particular matter.

“Credit Facility” means an irrevocable and unconditional letter of credit, a standby purchase agreement, a line of credit or other similar credit arrangement issued by a Qualified Bank to satisfy all or a portion of the Reserve Requirement.

“DTC” means the Depository Trust Company, New York, New York, or its successors and assigns as depository for the Bonds.

“Direct Participants” means those broker-dealers, banks and other financial institutions from time to time for which DTC holds Bonds as securities depository.

“Event of Default” means any of the events specified in Section 11.01 hereof.

“Federal Securities” mean any direct, noncallable obligations of the United States of America (including obligations issued or held in book-entry form on the books of the Department of the Treasury of the United States of America), or other noncallable obligations for which the faith and credit of the United States of America are pledged for the payment of principal and interest.

“Fitch” means Fitch Ratings, and its successors and assigns.

“Information Services” means Financial Information, Inc.’s “Daily Called Bond Service,” 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor; Mergent/FIS, Inc., 5250 77 Center Drive, Suite 150, Charlotte, North Carolina 28217, Attention: Called Bond Department; and Standard & Poor’s J.J. Kenny Drake, Inc., 55 Water Street, New York, New York 10041, Attention: Notification Department; and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses and/or such other services providing information with respect to called bonds as the Authority may designate in a Certificate of the Authority delivered to the Trustee.

“Installment Sale Agreement” means the Installment Sale Agreement, dated as of even date herewith, by and between the City and the Authority, as may be amended or supplemented from time to time.

“Insurance Paying Agent” means, with respect to the Series 2004 Bonds, _____, or its successors under the Bond Insurance Policy for such Bonds.

“Interest Account” means the account by that name in the Bond Fund established and held by the Trustee pursuant to Section 5.05.

“Interest Payment Date” means June 1 and December 1 of each year (beginning, with respect to the Series 2004 Bonds, June 1, 2005 and ending on the final maturity date of such Bonds).

“Maximum Annual Debt Service” means, with respect to the Bonds, the largest Annual Debt Service during the period from the date of calculation through the final maturity date of any Outstanding Bonds.

“Moody’s” means Moody’s Investors Services, its successors and assigns.

“Nominee” means the nominee of DTC, which initially shall be Cede & Co., or other nominee as DTC shall designate from time to time.

“Outstanding” means, when used with reference to Bonds, as of any date, Bonds theretofore or thereupon issued under this Trust Agreement except:

- (a) Bonds cancelled by the Trustee or delivered to the Trustee for cancellation at or prior to such date;

(b) Bonds (or portions of Bonds) deemed paid pursuant to Section 10.01 hereof;
or

(c) Bonds in lieu of or in substitution for which other Bonds shall have been prepared, executed and delivered pursuant to Article III hereof.

“Owner” means the registered owner of any Bond as shown on the Bond register to be maintained by the Trustee pursuant to Section 3.06 hereof.

“Permitted Investments” mean any of the following obligations if and to the extent that they are permissible investments of funds of the Authority and the City:

[to come]

() Any state administered pool investment fund in which the Authority and the City is statutorily permitted or required to invest will be deemed a permitted investment, including, but not limited to the Local Agency Investment Fund in the treasury of the State.

“Qualified Bank” means a state or national bank or trust company or a foreign bank with a domestic branch or agency which is organized and in good standing under the laws of the United States or any state thereof or any foreign country, which has a capital and surplus of \$25,000,000 or more and which has a short term debt rating of the highest ranking or of the highest letter and numerical rating as provided by Moody’s or by S&P.

“Principal Account” means the account by that name in the Bond Fund established and held by the Trustee pursuant to Section 5.05.

“Project Fund” means the fund by that name established and held by the Trustee pursuant to Section 5.03.

“Rating Agency” means Moody’s, Fitch, or any other national rating agency then maintaining a rating on the Bonds.

“Record Date” means with respect to any Interest Payment Date for a Bond the fifteenth (15th) day of the calendar month immediately preceding each Interest Payment Date.

“Redemption Date” means the date fixed for an optional or mandatory redemption, as the case may be, prior to maturity of the Bonds.

“Redemption Fund” means the fund by that name established and held by the Trustee pursuant to Section 5.10.

“Redemption Price” means a price equal to the principal amount represented by a Bond, plus the interest accrued to the applicable Redemption Date, plus premium, if applicable.

“Registration Books” means the records maintained by the Trustee pursuant to Sections 3.06 and 3.07 for the registration and transfer of ownership of the Bonds.

“Representation Letter” means the Blanket Issuer Letters of Representations, dated January 20, 2004, from the Authority to DTC.

“Reserve Account” means the account by that name in the Bond Fund established and held by the Trustee pursuant to Section 5.05.

“Reserve Account Policy” means a policy of insurance or surety bond issued by a municipal bond insurer or financial institution, obligations insured by which have a rating by Moody’s and S&P which at the time of issuance is the highest rating then issued by said Rating Agency, to satisfy all or a portion of the Reserve Requirement.

“Reserve Requirement” means, as of any calculation date, an amount equal to the least of (a) ten percent (10%) of the proceeds (within the meaning of Section 148 of the Code) of that portion of Bonds Outstanding with respect to which Annual Debt Service is calculated, (b) 125% of Average Annual Debt Service, or (c) Maximum Annual Debt Service; provided, that such Reserve Requirement or a portion thereof may be satisfied by one or more Reserve Account Policies or Credit Facilities upon the filing by the Authority or City with the Trustee of written evidence that the use of such Reserve Account Policy or Credit Facility to satisfy the Reserve Requirement or any portion thereof will not by itself result in the downgrading or withdrawal of any credit rating then in effect with respect to the Bonds.

“Revenues” mean (a) all amounts received by the Authority or the Trustee pursuant or with respect to the Installment Sale Agreement, including, without limiting the generality of the foregoing, all of the Installment Payments (including both timely and delinquent payments, any late charges, and whether paid from any source), prepayments, insurance proceeds, condemnation proceeds, and (b) all interest, profits or other income derived from the investment of amounts in any fund or account established pursuant to this Trust Agreement but excluding any Additional Payments.

“S&P” means Standard & Poor’s, a division of the McGraw-Hill Companies, Inc., and its successors and assigns.

“Securities Depositories” mean The Depository Trust Company, 55 Water Street, 50th Floor, New York, New York, 10041, Attn: Call Notification Department, Fax (212) 855-7232; or, in accordance with then-current guidelines of the Securities and Exchange Commission, such other securities depositories, or no such depositories, as the Authority may indicate in a Written Certificate of the Authority delivered to the Trustee.

“Serial Bonds” mean Bonds for which no mandatory sinking account payments are provided.

“Series” means, when used with reference to the Bonds, means all of the Bonds authenticated and delivered on original issuance and identified pursuant to this Trust Agreement (or a Supplemental Trust Agreement) authorizing such Bonds as a separate Series of Bonds, and any Bonds thereafter authenticated and delivered in lieu of or in substitution for such Bonds pursuant to the Trust Agreement.

“Series 2004 Bonds” mean the bonds authorized by Section 3.01 of this Trust Agreement and designated “Morgan Hill Financing Authority Water Revenue Bonds, Series 2004.”

“Series 2004 Project Account” means the account by that name within the Project Fund established and held by the Trustee pursuant to Section 5.03.

“Sinking Account” means the account by that name within the Bond Fund established and held by the Trustee pursuant to Section 5.05.

“State” means the State of California.

“Supplemental Trust Agreement” means any agreement supplemental to or amendatory of this Trust Agreement.

“Tax Certificate” means the Certificate Regarding Compliance with Certain Tax Matters (or similar instruments) pertaining to the use and investment of proceeds of a Series of Bonds, executed and delivered by a duly authorized officer of the Authority and of the City on the related Closing Date, including any and all exhibits and attachments thereto.

“Tax-exempt” means, with respect to interest on any obligations of a state or local government, including the interest on the Bonds, that such interest is excluded from gross income for federal income tax purposes (other than in the case of a holder of any such obligation who is a substantial user of the facilities financed with such obligations or a related person within the meaning of Section 147(a) of the Code) whether or not such interest is includable as an item of tax preference or otherwise includable directly or indirectly for purposes of calculating tax liabilities, including any alternative minimum tax or environmental tax, under the Code.

“Term Bonds” mean (i) the Series 2004 Bonds maturing on June 1, 20__ and June 1, 20__ and (ii) any other term Bonds issued pursuant to this Trust Agreement.

“Trust Agreement” means this Trust Agreement entered into by and between the Trustee and the Authority, as originally executed and entered into and as it may from time to time be amended or supplemented in accordance herewith.

“Trust Estate” means all estate, right, title and interest of the Trustee in and to all Revenues and the proceeds of the Bonds and all rights to enforce the Installment Payments under the Installment Sale Agreement, including, without limitation all amounts from time to time deposited in the funds, accounts and subaccounts created pursuant to this Trust Agreement and, to the extent set forth herein, investment earnings thereon.

“Written Certificate,” “Written Request” or “Written Requisition” of the Authority or the City mean, respectively, a written certificate, request or requisition signed in the name of the Authority or the City by its Authorized Representative. Any such instrument and supporting opinions or representations, if any, may, but need not, be combined in a single instrument with any other instrument, opinion or representation, and the two or more so combined shall be read and construed as a single instrument.

Section 1.02 Interpretation.

(a) Unless the context otherwise indicates, words expressed in the singular shall include the plural and vice versa and the use of the neuter, masculine, or feminine gender is for convenience only and shall be deemed to include the neuter, masculine or feminine gender, as appropriate.

(b) Headings of articles and sections herein and the table of contents hereof are solely for convenience of reference, do not constitute a part hereof and shall not affect the meaning, construction or effect hereof.

(c) All references herein to “Articles”, “Sections” and other subdivisions are to the corresponding Articles, Sections or subdivisions of this Trust Agreement unless otherwise indicated; the words “herein”, “hereof”, “hereby”, “hereunder” and other words of similar import refer to this Trust Agreement as a whole and not to any particular Article, Section or subdivision hereof.

ARTICLE II

DECLARATION OF TRUST

Section 2.01 Declaration of Trust. The Authority hereby establishes a trust and hereby grants, conveys, assigns and transfers the Trust Estate to the Trustee. The Trustee hereby declares that it holds and will hold the Trust Estate upon the trusts hereinafter set forth and for the use and benefit of the Owners, as more particularly set forth herein.

Section 2.02 Payments from Trust Estate Only; Distribution of Trust Estate. Except as otherwise expressly provided herein, all amounts payable by the Authority with respect to the Bonds pursuant to this Trust Agreement shall be paid only from the income of and proceeds from the Trust Estate and only to the extent that the Authority shall have actually received sufficient income or proceeds from the Trust Estate to make such payments in accordance with the terms of Article III. Each Owner agrees, except as otherwise expressly provided herein, to look solely to the income of and the proceeds from the Trust Estate to the extent available for distribution to such Owner as herein provided and that neither the Authority nor the Trustee is personally liable to any Owner for any amounts payable under this Trust Agreement.

ARTICLE III

BONDS, TERMS AND PROVISIONS

Section 3.01 Authorization of Bonds. The Authority hereby authorizes the issuance hereunder of the Series 2004 Bonds to be designated “Morgan Hill Financing Authority Water Revenue Bonds, Series 2004.” The initial aggregate principal amount of the Series 2004 Bonds shall be _____ Dollars (\$_____). The Series 2004 Bonds shall

constitute special obligations of the Authority, for the purpose of providing funds to the City to finance certain capital costs relating to the 2004 Projects. The Bonds issued under this Trust Agreement shall be designated generally as the "Morgan Hill Financing Authority Water Revenue Bonds." This Trust Agreement constitutes a continuing agreement with the Trustee and the Owners from time to time of the Bonds to secure the full payment of the principal of and interest and premium (if any) on all the Bonds, subject to the covenants, provisions and conditions herein contained.

(b) So long as the Installment Sale Agreement shall be in effect, all Installment Payments shall be paid by the City directly to the Trustee for application in accordance with this Trust Agreement.

Section 3.02 Terms of the Bonds. The Bonds shall be issued in fully registered form without coupons in denominations of \$5,000 or any integral multiple thereof.

The interest, principal, and redemption premiums, if any, due with respect to the Bonds shall be payable in lawful money of the United States of America. Subject to Section 3.13, the interest due on the Bonds shall be payable on their Interest Payment Dates by check or draft mailed by first class mail on the applicable Interest Payment Date by the Trustee to the respective Owners thereof at their addresses as they appear in the Registration Books on the Record Date with respect to each Interest Payment Date; provided, however, that payment of interest may be by wire transfer in immediately available funds to an account in the United States of America to any Owner of Bonds in the aggregate principal amount of \$1,000,000 or more who shall furnish written wire instructions to the Trustee at least five (5) days before the applicable Record Date. Principal of any Bond and any premium upon redemption shall be paid by check of the Trustee upon presentation and surrender thereof at the Corporate Trust Office of the Trustee.

Interest on the Bonds shall accrue on overdue principal at the same rate borne by the particular Bonds. Interest on each Bond shall accrue from the Interest Payment Date next preceding the date of authentication thereof unless (a) it is authenticated on an Interest Payment Date, in which event interest shall accrue from the date of authentication thereof; (b) it is authenticated on or prior to the Record Date preceding the first Interest Payment Date in which event interest shall accrue from its date; or (c) it is authenticated after a Record Date and prior to the next succeeding Interest Payment Date, in which case interest shall accrue from the next succeeding Interest Payment Date; provided, however, that if, at the time of authentication of any Bond, interest is in default on Outstanding Bonds, the Trustee shall establish a special record date for payment of any interest in default hereunder and interest on such Bond shall accrue from the date to which interest has previously been paid in full or made available for payment on such Outstanding Bonds. Interest on the Bonds will be computed on the basis of a 360-day year of twelve 30-day months.

Section 3.03 Series 2004 Bonds. (a) The Series 2004 Bonds shall be dated the Closing Date for such Bonds, shall mature on the dates and in the amounts and shall bear interest at the rates, as set forth below:

Maturity (June 1)	Principal Amount	Interest Rate
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Section 3.04 Execution and Authentication. (a) The Bonds shall be executed in the name of the Authority, by the manual or facsimile signature of the President or the Vice President of the Authority, and attested by the manual or facsimile signature of the Secretary of the Authority, or in such other manner as may be required or permitted by law. In case any one or more of the officers who shall have executed any of the Bonds shall cease to be an officer before the Bonds so executed shall have been delivered, such Bonds may nevertheless be delivered and, upon such delivery, shall be as binding as though such officer had continued to be an officer, and also any Bond may be executed on behalf of the Authority by any person who at the actual date of the execution of such Bond shall be an officer although at the nominal date of such Bond any such person shall not have been so authorized or have held such office.

(b) The Bonds shall bear thereon a certificate of authentication executed manually by the Trustee. At any time and from time to time after the execution and delivery of this Trust Agreement, the Authority may deliver Bonds executed by the Authority to the Trustee, together with a Written Request for the authentication and delivery of such Bonds; and the Trustee in accordance with such Written Request shall authenticate and deliver such Bonds as in this Trust Agreement provided. Only such Bonds as shall bear thereon such certificate of authentication, shall be entitled to any right or benefit under the Trust Agreement, and no Bond shall be valid or obligatory for any purpose until such certificate of authentication shall have been duly executed by the Trustee. Such certificate of the Trustee upon any Bond executed on behalf of the Authority shall be conclusive evidence that the Bond so authenticated has been duly authenticated and delivered under the Trust Agreement and that the Owner thereof is entitled to the benefits of the Trust Agreement.

Section 3.05 Exchange. Bonds, upon surrender thereof at the Corporate Trust Office of the Trustee, may, at the option of the Owner and upon payment by such Owner of any charges which the Trustee may make as provided in Section 3.08 hereof, be exchanged for an

equal aggregate principal amount of registered Bonds of the same maturity, tenor and Series of any other authorized denominations.

Section 3.06 Negotiability, Transfer and Registry. (a) Each Bond shall be transferable only upon the books of the Trustee which shall be kept for that purpose at the Corporate Trust Office of the Trustee, by the Owner in person or by his attorney duly authorized in writing, upon surrender thereof together with a written instrument of transfer satisfactory to the Trustee duly executed by the Owner or such Owner's duly authorized attorney and upon payment by such Owner of any charges which the Trustee may make as provided in Section 3.08 hereof. Upon the transfer of any such Bond the Trustee shall execute and deliver in the name of the transferee a new Bond or Bonds of the same principal amount, series, tenor and maturity as the surrendered Bond.

(b) The Trustee may deem and treat the person in whose name any Bond shall be registered upon the books of the Trustee as the absolute Owner of such Bond, whether such Bond shall be overdue or not, for the purpose of receiving payment of, or on account of, the principal and premium, if any, and interest with respect to such Bond and for all other purposes, and all such payments so made to any such Owner or upon his order shall be valid and effectual to satisfy and discharge the liability upon such Bond to the extent of the sum or sums so paid, and the Trustee shall not be affected by any notice to the contrary.

(c) The Trustee shall not be required to transfer or exchange (i) any Bond in the fifteen (15) days prior to selection of Bonds for redemption (whether or not such Bond is thereafter selected for redemption) and (ii) any Bond selected for redemption in whole or in part.

Section 3.07 Bond Registration Books. The Trustee shall keep at its Corporate Trust Office sufficient Registration Books for the registration of the ownership, transfer and exchange of the Bonds, which Registration Books shall be available for inspection by the Authority and its designated agent or any Owner or such Owner's agent duly authorized in writing at reasonable hours and under reasonable conditions; and upon presentation for such purpose the Trustee shall, under such reasonable regulations as it may prescribe, register the ownership, transfer or exchange of the Bonds in such Registration Books as hereinabove provided. The ownership of any Bonds may be proved by the Registration Books.

Section 3.08 Additional Provisions with Respect to Exchanges and Transfers. In all cases in which the privilege of exchanging Bonds or transferring Bonds is exercised, the Trustee shall execute and deliver Bonds in accordance with the provisions of this Trust Agreement. All Bonds surrendered in any such exchanges or transfers shall forthwith be cancelled by the Trustee and destroyed, and the Trustee shall certify as to their destruction. For every such exchange or transfer of Bonds, whether temporary or definitive, the Trustee may make a charge to the Owners thereof sufficient to reimburse it for any tax, or other governmental charge required to be paid with respect to such exchange or transfer.

Section 3.09 Bonds Mutilated, Destroyed, Stolen or Lost. In case any Bond shall become mutilated or be destroyed, stolen or lost, the Trustee shall execute and deliver, a new Bond of like maturity, Series and principal amount as the Bond so mutilated, destroyed, stolen or lost, in exchange and substitution for such mutilated Bond, upon surrender and

cancellation of such mutilated Bond, or in lieu of and substitution for the Bond destroyed, stolen or lost, upon filing with the Trustee evidence satisfactory to the Trustee that such Bond has been destroyed, stolen or lost and proof of ownership thereof, and upon furnishing the Trustee with indemnity satisfactory to the Trustee and complying with such other reasonable regulations as the Trustee may prescribe and paying such expenses as the Trustee may incur. All Bonds so surrendered to the Trustee shall be cancelled by it and destroyed, and the Trustee shall certify in writing as to their destruction. Any such new Bonds issued pursuant to this Section 3.09 in substitution for Bonds alleged to be destroyed, stolen or lost shall be entitled to equal and proportionate benefits, with all other Bonds delivered under this Trust Agreement, in any moneys or security held by the Trustee for the benefit of the Owners.

Section 3.10 Temporary Bonds. (a) Until definitive Bonds are prepared, the Authority may direct the Trustee to authenticate and deliver, in the same manner as is provided in this Article III, in lieu of definitive Bonds, one or more temporary Bonds substantially of the tenor of the definitive Bonds in lieu of which such temporary Bond or Bonds are issued, in denominations authorized hereunder, so long as no such Bond shall have its principal amount becoming payable in more than one year, and with such omissions, insertions and variations as may be appropriate to temporary Bonds. At the expense of the Authority, the Authority shall prepare and the Trustee shall authenticate and, upon the surrender of such temporary Bonds and the cancellation of such surrendered temporary Bonds, the Trustee shall without charge to the Owner thereof, in exchange therefor, deliver definitive Bonds, of the same principal amount, Series and maturity as the temporary Bonds surrendered. Until so exchanged, the temporary Bonds shall in all respects be entitled to the same benefits and security as definitive Bonds executed and delivered pursuant to this Trust Agreement.

(b) If the Authority shall request the execution and delivery of temporary Bonds in more than one denomination, the Owner of any temporary Bond or Bonds may, at his option, surrender the same to the Trustee in exchange for another temporary Bond or Bonds of like principal amount, Series and maturity of any other authorized denomination or denominations, and thereupon the Trustee shall authenticate and deliver, in exchange for the temporary Bond or Bonds so surrendered and upon payment of the taxes, fees and charges provided for in Section 3.08 hereof, a temporary Bond or Bonds of like aggregate principal amount, Series and maturity in such other authorized denomination or denominations as shall be requested by such Owner.

(c) All temporary Bonds surrendered in exchange either for another temporary Bond or Bonds or for a definitive Bond or Bonds shall be forthwith cancelled by the Trustee and destroyed, and the Trustee shall certify in writing as to their destruction.

Section 3.11 Cancellation of Bonds. All Bonds paid or redeemed, either at or before maturity, shall be delivered to the Trustee when such payment or redemption is made and such Bonds shall thereupon be promptly cancelled and destroyed, and the Trustee shall certify in writing as to their destruction.

Section 3.12 Bond Form. The form of the Series 2004 Bonds to be issued under this Trust Agreement, the form of Trustee's certificate of authentication and the form of assignment are to be substantially as set forth in Exhibit A attached hereto, with necessary and

appropriate variations, omissions and insertions as permitted or required by this Trust Agreement.

Section 3.13 Book-Entry Only System.

(a) Notwithstanding the foregoing provisions of this Article III, except as otherwise provided in subsections (b) and (c) of this Section 3.13, the Bonds initially authenticated and delivered hereunder shall be registered in the name of the Nominee, as Nominee of DTC, or such other Nominee as DTC shall request. Payments of interest on, principal of and any premium on the Bonds shall be made to the account of the Nominee on each payment date for principal or interest on the Bonds at the address indicated for the Nominee in the Registration Books by transfer of immediately available funds. DTC has represented to the Authority that it will maintain a book-entry system in recording ownership interests of the Direct Participants and the ownership interests of Beneficial Owners will be recorded through book entries on the records of the Direct Participants.

(b) The Bonds shall be initially issued in the form of a separate single authenticated fully registered Bond for each maturity of the Bonds. With respect to Bonds so registered in the name of the Nominee, the Authority and the Trustee shall have no responsibility or obligation to any Direct Participant or to any Beneficial Owner of such Bonds. Without limiting the immediately preceding sentence, the Authority and the Trustee shall have no responsibility or obligation with respect to (i) the accuracy of the records of DTC, the Nominee or any Direct Participant with respect to any beneficial ownership interest in the Bonds, (ii) the delivery to any Direct Participant, Beneficial Owner or other person, other than DTC, of any notice with respect to the Bonds, including any notice of redemption, (iii) the payment to any Direct Participant, Beneficial Owner or other person, other than DTC, of any amount with respect to the principal or redemption price of, or interest on, the Bonds, or (iv) any consent given or other action taken by DTC as Owner of the Bonds. The Authority and the Trustee may treat DTC as, and deem DTC to be, the absolute Owner of each Bond for all purposes whatsoever including (but not limited to) (I) payment of the principal or redemption price of, and interest on, each such Bond, (II) giving notices of conversion or redemption and other matters with respect to such Bonds and (III) registering transfers with respect to such Bonds. The Trustee shall pay the principal or redemption price of, and interest on, all book-entry Bonds only to or upon the order of DTC, and all such payments shall be valid and effective to fully satisfy and discharge the Authority's obligations with respect to such principal or redemption price, and interest, to the extent of the sum or sums so paid. No person other than DTC shall receive a Bond evidencing the obligation of the Authority to make payments of principal or redemption price of, and interest on, the Bonds pursuant to this Trust Agreement.

(c) DTC may determine to discontinue providing its services with respect to the Bonds at any time by giving reasonable written notice to the Authority and the Trustee and discharge its responsibilities with respect thereto under applicable law. The Authority, in its sole discretion, may terminate, upon provision of notice to the Trustee, the services of DTC with respect to the Bonds. In the event (i) DTC determines not to continue to act as securities depository for the Bonds, or (ii) the Authority determines that DTC shall no longer so act, then the Authority will discontinue the book-entry system with the DTC. If the Authority fails to identify another qualified securities depository to replace the DTC, then the Bonds so designated

shall no longer be restricted to being registered in the Registration Books in the name of the Nominee, or any other nominee of DTC, but shall be registered in whatever name or names persons transferring or exchanging Bonds shall designate, in accordance with the provisions of Section 3.05 through 3.10.

(d) In order to qualify the Bonds for DTC's book-entry system, the Authority has executed and delivered the Representation Letter to DTC. The Representation Letter shall not in any way impose upon the Authority or the Trustee any obligation whatsoever with respect to persons having interests in the Bonds other than the Owners, as shown on the Registration Books. The Trustee agrees to take all action necessary to continuously comply with the Representation Letter to the extent that such action is not inconsistent with this Trust Agreement.

(e) Notwithstanding any provision herein to the contrary, the Authority and the Trustee may agree to allow DTC, or its Nominee, to make a notation on any Bond redeemed in part to reflect, for information purposes only, the principal amount and date of any such redemption.

ARTICLE IV

REDEMPTION OF BONDS

Section 4.01 Terms of Redemption for Series 2004 Bonds.

(a) **Sinking Account Redemption.** The Series 2004 Bonds maturing on June 1, 20__ are subject to mandatory redemption in part by lot from Sinking Account payments on June 1 of each year commencing on June 1, 20__ as set forth in the following schedule. All redemptions pursuant to the preceding sentence shall be at a redemption price equal to the principal amount thereof to be redeemed (without premium), together with interest accrued thereon to the date fixed for redemption; provided, that if some but not all of the Term Bonds of a maturity have been optionally redeemed pursuant to subsection (b) below, each future Sinking Account payment with respect to such Term Bonds will be reduced on a pro rata basis (as nearly as practicable) in integral multiples of \$5,000, so that the total amount of Sinking Account payments with respect to such Term Bonds to be made subsequent to the optional redemption shall be reduced in by amount equal to the principal amount of the Term Bonds so redeemed, all as shall be designated pursuant to written notice filed by the Authority with the Trustee.

Series 2004 Bonds Maturing June 1, 20__	
Redemption Date	Principal Amount
<u>(June 1)</u>	<u>to be Redeemed</u>

In lieu of such redemption, the Trustee may apply amounts in the Sinking Account to purchase Term Bonds at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Account) as may be directed by the Authority, except that the purchase price (exclusive of accrued interest) may not exceed the redemption price then applicable to such Series 2004 Bonds, as set forth in a Written Request of the Authority; provided, however, that no Term Bonds shall be purchased by the Trustee hereunder with a settlement date more than 60 days prior to the date on which the Authority would otherwise redeem such Term Bonds pursuant to this Section 4.01(a). The principal amount of any Term Bonds so purchased by the Trustee shall be credited towards and shall reduce the Sinking Account payment otherwise required to be made with respect to such Term Bonds on the applicable redemption date.

(b) **Optional Redemption.** The Series 2004 Bonds maturing on or before June 1, 20[14] shall not be subject to optional redemption by the Authority. The Series 2004 Bonds maturing on or after June 1, 20[15] shall be subject to redemption at the option of the Authority, as a whole or in part on any Interest Payment Date on or after June 1, 20[14], from any available source of funds (including, but not limited to, prepayments made by the City pursuant to Section 3.02(a) of the Installment Sale Agreement), upon no less than 45 days written notice to the Trustee, at a redemption price equal to [100] percent of the principal amount of the Series 2004 Bonds to be redeemed, together with accrued interest thereon to the date fixed for redemption[, with no premium].

Section 4.02 Selection of Bonds for Redemption. Whenever provision is made in this Trust Agreement for the redemption of less than all of the Bonds of any Series, the Trustee shall select the Bonds to be redeemed from all Outstanding Bonds of such Series or such given portion thereof not previously called for redemption, among maturities (unless the maturity or maturities are otherwise specified in this Trust Agreement or in the related Written Request of the Authority) and by lot within a maturity in any manner which the Trustee in its discretion shall deem appropriate. For purposes of such selection, the Trustee shall treat each Bond as consisting of separate \$5,000 portions and each such portion shall be subject to redemption as if such portion were a separate Bond.

Section 4.03 Notice of Redemption. Notice of redemption shall be mailed by first class mail, postage prepaid, not less than thirty (30) nor more than sixty (60) days before any redemption date, to the respective Owners of any Bonds designated for redemption at their addresses appearing on the Registration Books, and to the Securities Depositories and to the Information Services. Each notice of redemption shall state the date of the notice, the redemption date, the place or places of redemption (including any name and appropriate address or addresses), whether less than all of the Bonds of a Series (or all Bonds of a single maturity within a Series) are to be redeemed, the Series designation, CUSIP numbers and Bond numbers of the Bonds to be redeemed, the maturity or maturities of the Bonds to be redeemed and in the case of Bonds of a single maturity to be redeemed in part only, the respective portions of the

principal amount thereof to be redeemed, and the redemption premium, if any. Each such notice shall also state that on the redemption date there will become due and payable on each of said Bonds the redemption price thereof, and that from and after such redemption date interest thereon shall cease to accrue, and shall require that such Bonds be then surrendered. Neither the failure to receive any notice nor any defect therein shall affect the proceedings or such redemption or the cessation of accrual of interest from and after the redemption date. Notice of redemption of Bonds shall be given by the Trustee, at the expense of the Authority, for and on behalf of the Authority.

Section 4.04 Partial Redemption of Bonds. Upon surrender of any Bonds redeemed in part only, the Authority shall execute and the Trustee shall authenticate and deliver to the Owner thereof, at the expense of the Authority, a new Bond or Bonds of authorized denominations equal in aggregate principal amount to the unredeemed portion of the Bonds surrendered.

Section 4.05 Effect of Redemption. Notice of redemption having been duly given as aforesaid, and moneys for payment of the redemption price of, together with interest accrued to the date fixed for redemption on, the Bonds (or portions thereof) so called for redemption being held by the Trustee, on the redemption date designated in such notice, the Bonds (or portions thereof) so called for redemption shall become due and payable, interest on the Bonds so called for redemption shall cease to accrue, said Bonds (or portions thereof) shall cease to be entitled to any benefit or security under this Trust Agreement, and the Owners of said Bonds shall have no rights in respect thereof except to receive payment of the redemption price thereof.

All Bonds redeemed pursuant to the provisions of this Article shall be cancelled by the Trustee upon surrender thereof and destroyed.

Section 4.06 Right to Rescind Optional Redemption. Notwithstanding the foregoing, an optional redemption pursuant to Section 4.01(b) may be rescinded upon receipt by the Trustee on or before the date fixed for redemption of (i) a written notice of rescission from the Authority, or (ii) a written notice from the City rescinding its optional prepayment of Installment Payments pursuant to Section 3.02(a) of the Installment Payment Agreement. Any notice of redemption shall be cancelled and annulled if for any reason funds will not be available on the date fixed for redemption for payment in full of the Bonds then called for redemption, and such cancellation shall not constitute an Event of Default hereunder. None of the Authority, the City or the Trustee shall have any liability to the Owners or any other party related to or arising from such rescission. The Trustee shall mail notice of such rescission in the same manner as that prescribed in Section 4.03.

ARTICLE V

APPLICATION OF PROCEEDS; ESTABLISHMENT AND ADMINISTRATION OF CERTAIN FUNDS AND ACCOUNTS

Section 5.01 Application of Series 2004 Bonds Proceeds. The proceeds received from the sale of the Series 2004 Bonds shall be deposited in trust with the Trustee, who shall forthwith set aside such proceeds as follows:

(a) The Trustee shall deposit the amount of \$_____ in the Series 2004 Costs of Issuance Account of the Costs of Issuance Fund;

(b) The Trustee shall deposit the amount of \$_____ in the Reserve Account, representing the full amount of the Reserve Requirement calculated as of the Closing Date for the Series 2004 Bonds; and

(c) The Trustee shall deposit the remaining balance of such proceeds, in the amount of \$_____, in the Series 2004 Project Account to be applied as provided in Section 5.03.

Section 5.02 Establishment and Application of Costs of Issuance Fund. The Trustee shall establish, maintain and hold in trust a separate fund designated as the "Costs of Issuance Fund." For the Series 2004 Bonds issued hereunder, the Trustee shall establish, maintain and hold an account within the Costs of Issuance Fund designated as "Series 2004 Costs of Issuance Account." For each other Series of Bonds issued hereunder, the Trustee shall establish, maintain and hold an account within the Costs of Issuance Fund designated as "Series _____ Costs of Issuance Account." All proceeds of each Series of Bonds deposited in the Costs of Issuance Funds shall be held in the account for such Series of Bonds and shall be accounted for separately from all other amounts in the Costs of Issuance Fund. The moneys in each account of the Costs of Issuance Fund shall be used and withdrawn by the Trustee to pay the Costs of Issuance for the related Series of Bonds upon submission of Written Requisitions of the Authority stating the person to whom payment is to be made, the amount to be paid, the purpose for which the obligation was incurred and that such payment is a proper charge against Costs of Issuance Fund. On the 120th day after the Closing Date of a Series of Bonds, or upon the earlier Written Request of the Authority, the Trustee shall transfer all amounts remaining in the related account in the Costs of Issuance Fund to the account in the Projects Fund established in connection with such Series of Bonds.

Section 5.03 Project Fund. The Trustee shall establish, maintain and hold in trust a separate fund to be known as the "Project Fund." For the Series 2004 Bonds issued hereunder, the Trustee shall establish, maintain and hold an account within the Project Fund designated as the "Series 2004 Project Account." For each other Series of Bonds issued hereunder, the Trustee shall establish, maintain and hold an account within the Project Fund designated as the "Series _____ Project Account." Except as otherwise provided herein, moneys in the Series 2004 Project Account shall be used solely for the payment of 2004 Project Costs. The Trustee shall disburse moneys in the Series 2004 Project Account from time to time to pay 2004 Project Costs (or to reimburse the City for payment of 2004 Project Costs) upon receipt by

the Trustee of a Written Requisition of the City which: (a) states with respect to each disbursement to be made (i) the requisition number, (ii) the name and address of the person, firm or corporation to whom payment will be made, (iii) the amount to be disbursed, (iv) that each obligation mentioned therein is a proper charge against the Series 2004 Project Account and has not previously been disbursed by the Trustee from amounts in the Series 2004 Project Account, (v) that the City has complied with the provisions of Section 4.03 of the Installment Sale Agreement, and (vi) that the amount of such disbursement is for 2004 Project Costs as defined in the Installment Sale Agreement; (b) specifies in reasonable detail the nature of the obligation; (c) is accompanied by a bill or statement of account (if any) for each obligation; (d) specifies the date (which shall be a Business Day) on which the transfer of such money shall be made. Upon the filing with the Trustee of a Written Certificate of the City stating that the 2004 Projects have been completed or that all Written Requisitions intended to be filed by the City have been filed, the Trustee shall withdraw all amounts then on deposit in the Series 2004 Project Account (other than the amount, if any, specified by the City in the Written Certificate to hold on deposit in the Project Fund for payments of 2004 Project Costs thereafter intended to be requisitioned by the City) and transfer such amounts to the Bond Fund; provided, that if the City elects to apply all or a portion of the balance in the Series 2004 Project Account to make an optional prepayment of Installment Payments pursuant to Sections 4.03 and 3.02 of the Installment Sale Agreement, then the Trustee shall transfer the amount specified by the City to the Redemption Fund to effect the corresponding optional redemption of the Bonds under Section 4.01(b) prior to making the transfer to the Bond Fund.

Notwithstanding the foregoing provisions of this Section 5.03, upon the occurrence and continuation of an Event of Default under and as defined in Section 11.01, the Trustee shall immediately withdraw all amounts then on deposit in the Project Fund and apply such amounts in accordance with the provisions of Section 11.03.

Section 5.04 Pledge and Assignment; Bond Fund.

(a) Subject only to the provisions of this Trust Agreement permitting the application thereof for the purposes and on the terms and conditions set forth herein, all of the Revenues are hereby pledged to secure the payment of the principal of and interest on the Bonds in accordance with their terms and the provisions of this Trust Agreement. Said pledge shall constitute a lien on and security interest in such assets and shall attach, be perfected and be valid and binding from and after the Closing Date, without any physical delivery thereof or further act.

(b) The Authority hereby transfers in trust, grants a security interest in and assigns to the Trustee, for the benefit of the Owners from time to time of the Bonds, all of the Revenues and all of the rights of the Authority in the Installment Sale Agreement (other than the rights of the Authority under Sections 3.03, 7.02 and 8.04 thereof). The Trustee shall be entitled to and shall collect and receive all of the Revenues, and any Revenues collected or received by the Authority shall be deemed to be held, and to have been collected or received, by the Authority as the agent of the Trustee and shall forthwith be paid by the Authority to the Trustee. The Trustee also shall be entitled to and shall, subject to the provisions of Articles XI and XII, take all steps, actions and proceedings which the Trustee determines to be reasonably necessary in its judgment to enforce, either jointly with the Authority or separately, all of the rights of the Authority and all of the obligations of the City under the Installment Sale Agreement.

The assignment of the Authority's rights under the Installment Sale Agreement to the Trustee is solely in its capacity as Trustee under this Trust Agreement and the duties, powers and liabilities of the Trustee in acting thereunder shall be subject to the provisions of this Trust Agreement. The Trustee shall not be responsible for any representations, warranties, covenants or obligations of the Authority.

(c) All Revenues shall be promptly deposited by the Trustee upon receipt thereof in a special fund designated as the "Bond Fund" which the Trustee shall establish, maintain and hold in trust; except that all moneys received by the Trustee and required hereunder or under the Installment Sale Agreement to be deposited in the Redemption Fund shall be promptly deposited in such Fund. All Revenues deposited with the Trustee shall be held, disbursed, allocated and applied by the Trustee only as provided in this Trust Agreement.

Section 5.05 Allocation of Revenues. Not later than the date on which principal of or interest on the Bonds becomes due and payable, the Trustee shall transfer from the Bond Fund and deposit into the following respective accounts (each of which the Trustee shall establish and maintain within the Bond Fund), the following amounts in the following order of priority, the requirements of each such account (including the making up of any deficiencies in any such account resulting from lack of Revenues sufficient to make any earlier required deposit) at the time of deposit to be satisfied before any transfer is made to any account subsequent in priority:

(a) The Trustee shall deposit in the Interest Account an amount required to cause the aggregate amount on deposit in the Interest Account to be at least equal to the amount of interest becoming due and payable on such date on all Bonds then Outstanding.

(b) The Trustee shall deposit in the Principal Account an amount required to cause the aggregate amount on deposit in the Principal Account to equal the principal amount of the Bonds coming due and payable on such date.

(c) The Trustee shall deposit in the Sinking Account an amount equal to the aggregate principal amount of the Term Bonds required to be redeemed on such date, if any, pursuant to Section 4.01(a).

(d) The Trustee shall deposit in the Reserve Account an amount, if any, required to cause the amount on deposit in the Reserve Account to be equal to the Reserve Requirement.

On or before June 15 and December 15 of each year the Trustee shall determine the amount, if any, remaining in the Bond Fund after making the deposits required by paragraphs (a) through (d) above and shall notify the City of the amount so determined. The Trustee shall apply such amount as a credit against the next following Installment Payments due from the City; provided that, if directed in a Written Request of the City, the Trustee shall, with respect to all or any portion of such amount, (i) pay, or set an amount aside for the payment of, rebate in accordance with a computation made by the City pursuant to Section 6.05 of the Installment Sale Agreement; (ii) transfer an amount to the Project Fund, or (iii) transfer to the City to be used for any lawful purpose.

Section 5.06 Application of Interest Account. All amounts in the Interest Account shall be used and withdrawn by the Trustee solely for the purpose of paying interest on the Bonds as it shall become due and payable (including accrued interest on any Bonds purchased or redeemed prior to maturity pursuant to this Trust Agreement).

Section 5.07 Application of Principal Account. All amounts in the Principal Account shall be used and withdrawn by the Trustee solely to pay the principal amount of the Bonds at their respective maturity dates.

Section 5.08 Application of Sinking Account. All moneys on deposit in the Sinking Account shall be used and withdrawn by the Trustee for the sole purpose of redeeming or purchasing (in lieu of redeeming) Term Bonds pursuant to Section 4.01(a).

Section 5.09 Application of Reserve Account. All amounts in the Reserve Account shall be used and withdrawn by the Trustee solely for the purpose of (a) paying interest on or principal of the Bonds, when due and payable to the extent that moneys deposited in the Interest Account or Principal Account, respectively, are not sufficient for such purpose, (b) paying the redemption price of any Term Bonds to be redeemed pursuant to Section 4.01(a) in the event that amounts on deposit in the Principal Account are not sufficient for such purpose, and (c) making the final payments of principal of and interest on the Bonds. On the date on which all Bonds shall be retired hereunder or provision made therefor pursuant to Article X, all moneys then on deposit in the Reserve Account shall be withdrawn by the Trustee and paid to the City. In the event of any deficiency in the Reserve Account (whether due to a payment therefrom or due to the fluctuation in market value of securities credited thereto, or otherwise) as of the fifteenth (15th) day of the month preceding any Interest Payment Date, the Trustee shall promptly notify the City in writing of the amount of such deficiency. Any amounts on deposit in the Reserve Account at any time in excess of the Reserve Requirement shall be transferred to the Bond Fund.

Section 5.10 Application of Redemption Fund. The Trustee shall establish and maintain the Redemption Fund, amounts in which shall be used and withdrawn by the Trustee solely for the purpose of paying the principal of and premium, if any, on the Bonds to be redeemed pursuant to Section 4.01(b).

Section 5.11 Investments. (a) All money held by the Trustee in any of the accounts or funds established pursuant hereto shall be invested in Permitted Investments at the Written Request of the Authority filed with the Trustee which Permitted Investments shall, as nearly as practicable, mature (or be subject to redemption or disposition by the Trustee) on or before the dates on which such money is anticipated to be needed for disbursement hereunder. If no such Written Request of the Authority is received by the Trustee, the Trustee shall invest such money in those Permitted Investments described in clause (d) of the definition thereof. The Trustee shall not be liable for any loss from any Permitted Investments acquired, held or disposed of in compliance with this Section 5.11.

(b) All interest or gain derived from the investment of amounts in any of the funds or accounts established hereunder shall be deposited in the Bond Fund, provided, however, that earnings on the investment of amounts in the Project Fund shall be retained therein and

earnings on the investment of the amount in the Reserve Account shall be retained therein to the extent required to maintain the Reserve Requirement.

(c) The Trustee or any of its affiliates may act as principal or agent, sponsor, advisor, or manager in connection with any investments made by the Trustee hereunder.

(d) The Authority acknowledges that to the extent regulations of the Comptroller of the Currency or other applicable regulatory entity grant the Authority the right to receive brokerage confirmations of security transactions as they occur, the Authority specifically waives receipt of such confirmations to the extent permitted by law. The Trustee will furnish the Authority monthly cash transaction statements which include detail for all investment transactions made by the Trustee hereunder.

Section 5.12 Valuation and Disposition of Investments. For the purpose of determining the amount in any fund or account established hereunder, any investments credited to such fund or account shall be valued at least annually, on or before June 30, at the market value thereof. In making any valuations hereunder the Trustee may utilize computerized securities pricing services that may be available to it, including those available through its regular accounting system.

ARTICLE VI

ISSUANCE OF ADDITIONAL BONDS

Section 6.01 Conditions to Issuance of Additional Bonds. Subsequent to the execution and delivery by the Trustee of the Series 2004 Bonds, the Trustee shall, upon Written Request of the Authority, execute and deliver from time to time one or more Series of Additional Bonds representing such aggregate principal amount as may be set forth in such Written Request, provided that the following conditions precedent shall have been satisfied:

(a) A Written Certificate of the City that the City has complied with all of the conditions set forth in Section 5.01 of the Installment Sale Agreement which are hereby made conditions precedent to the preparation, execution and delivery of such Additional Bonds;

(b) The parties to this Trust Agreement shall have executed a Supplemental Trust Agreement setting forth the terms and provisions of such Additional Bonds, including the establishment of such funds and accounts, separate and apart from the funds and accounts established hereunder for the Series 2004 Bonds, as shall be necessary or appropriate;

(c) The scheduled principal and interest payments with respect to such Additional Bonds and payable only on Interest Payment Dates applicable to the Series 2004 Bonds;

(d) The Installment Sale Agreement shall have been amended by the parties thereto, in accordance with its terms, to (i) increase or adjust the payments due and payable on each Interest Payment Date to an amount sufficient

to pay the principal, premium (if any) and interest payable with respect to all Outstanding Bonds, including all Additional Bonds as and when such principal and interest matures or becomes due and payable, and (ii) make such other revisions to the Installment Sale Agreement as are necessitated by the execution and delivery of such Additional Bonds (provided, however, that such other revisions shall not prejudice the rights of the Owners of Outstanding Bonds to payments under the terms of this Trust Agreement);

(e) There shall have been delivered to the Trustee a counterpart of the amendments required by subsection (d) above;

(f) Provisions shall have been made for the deposit into the Reserve Account of an amount, if any, necessary to increase the balance therein to the Reserve Requirement, as calculated at the time such Additional Bonds are issued;

(g) The Trustee shall have received an Written Certificate of the Authority that there exists on the part of the Authority no Event of Default; and

(h) The Trustee shall have received an opinion of Bond Counsel to the effect that (i) said Supplemental Trust Agreement and said amendments to the Installment Sale Agreement comply in all respects with the requirements of this Section 6.01; (ii) said Supplemental Trust Agreement and said amendments to the Installment Sale Agreement have been duly authorized, executed and delivered by each of the respective parties thereto (provided that said opinion of Counsel, in rendering the opinions set forth in this clause (ii), shall be entitled to rely upon one or more other opinions of Counsel, including counsel to any of the respective parties to said Supplemental Trust Agreement or said Installment Sale Agreement); and (iii) the execution and delivery of such Supplemental Trust Agreement and said amendments to the Installment Sale Agreement, and performance by the parties thereunder, does not adversely affect the exclusion from gross income under the Code or the exemption under State law of the interest on the then Outstanding Bonds.

Section 6.02 Execution and Delivery of Additional Bonds. Upon the satisfaction of the conditions precedent set forth in Section 6.01, the Trustee shall cause to be executed and delivered Additional Bonds representing the aggregate principal amount specified in such Supplemental Trust Agreement, and such Additional Bonds shall be equally and ratably secured with all Bonds, including any Additional Bonds, theretofore prepared, executed and delivered, all without preference, priority or distinction (other than with respect to maturity, payment, redemption or sinking account payments (if any)) of any one Bond, including Additional Bonds, over any other; provided, however, that no provision of this Trust Agreement shall require the Authority to consent to or otherwise permit the preparation, execution and delivery of Additional Bonds, it being understood and agreed that any such consent or other action of the Authority to permit the preparation, execution and delivery of Additional Bonds, or lack thereof, shall be in the sole discretion of the Authority.

ARTICLE VII

COVENANTS OF AUTHORITY AND TRUSTEE

Section 7.01 Compliance. The Authority covenants that it will observe and faithfully perform at all times all of its covenants, undertakings and agreements contained in this Trust Agreement and the Installment Sale Agreement.

Section 7.02 Observance of Laws and Regulations. The Authority and the Trustee will faithfully comply with, keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America or of the State of California, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of each and every franchise, right or privilege now owned or hereafter acquired by them, including their right to exist and carry on their respective businesses, to the end that such franchises, rights and privileges shall be maintained and preserved and shall not become abandoned, forfeited or in any manner impaired.

Section 7.03 Tax Covenants. (a) The Authority hereby covenants that, notwithstanding any other provisions of this Trust Agreement, it shall not take any action, or fail to take any action, if any such action or failure to take action would adversely affect the Tax-exempt status of interest on the Bonds under Section 103 of the Code. The Authority shall not, directly or indirectly, use or permit the use of proceeds of the Bonds or any of the property financed or refinanced with proceeds of the Bonds, or any portion thereof, by any person other than a governmental unit (as such term is used in Section 141 of the Code), in such manner or to such extent as would adversely affect the Tax-exempt status of interest on the Bonds.

(b) The Authority shall not take any action, or fail to take any action, if any such action or failure to take action would cause the Bonds to be “private activity bonds” within the meaning of Section 141 of the Code, and in furtherance thereof, shall not make any use of the proceeds of the Bonds or any of the property financed or refinanced with proceeds of the Bonds, or any portion thereof, or any other funds of the Authority, that would cause the Bonds to be “private activity bonds” within the meaning of Section 141 of the Code. To that end, so long as any Bonds are Outstanding, the Authority, with respect to such proceeds and property and such other funds, will comply with applicable requirements of the Code and all regulations of the United States Department of the Treasury issued thereunder, to the extent such requirements are, at the time, applicable and in effect.

(c) The Authority shall not, directly or indirectly, use or permit the use of any proceeds of any Bonds, or of any property financed or refinanced thereby, or other funds of the Authority, or take or omit to take any action, that would cause the Bonds to be “arbitrage bonds” within the meaning of Section 148 of the Code. To that end, the Authority shall comply with all requirements of Section 148 of the Code and all regulations of the United States Department of the Treasury issued thereunder to the extent such requirements are, at the time, in effect and applicable to the Bonds.

(d) The Authority shall not make any use of the proceeds of the Bonds or any other funds of the Authority, or take or omit to take any other action, that would cause the Bonds to be “federally guaranteed” within the meaning of Section 149(b) of the Code.

(e) In furtherance of the foregoing tax covenants, the Authority covenants that it will comply with the provisions of the Tax Certificate, which is incorporated herein as if fully set forth herein. These covenants shall survive payment in full or defeasance of the Bonds.

Section 7.04 Account Records and Statements. The Trustee will keep or cause to be kept proper books of record and accounts in which complete and correct entries shall be made of all transactions made by the Trustee relating to the receipts, disbursements, allocation and application of the Installment Payments and the proceeds of the Bonds, and such books shall be available for inspection by the Authority, at reasonable hours and under reasonable conditions.

Section 7.05 Recording and Filing. The Trustee upon receipt of a Written Request of the Authority shall, at the expense of the Authority, file, record, register, renew, refile and rerecord all such documents, including financing statements (or continuation statements in connection therewith), all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to fully perfect, preserve and protect the security of the Owners and the rights and interests of the Trustee; provided, however, that the Trustee will not be required to execute a special or general consent to service of process, or to qualify as a foreign corporation in connection with any such filing, recording, registration, refile or rerecording in any jurisdiction in which it is not now so subject.

Section 7.06 Amendment of Installment Sale Agreement. The Authority shall not amend, supplement or otherwise modify or consent to the amendment, supplement or modification, in whole or in part, of the Installment Sale Agreement except:

(a) to the extent such amendment, alteration or modification shall cure an ambiguity, supply an omission, or cure or correct a defect or inconsistent provision therein;

(b) to the extent such amendment, alteration or modification shall insert such provisions clarifying matters or questions arising thereunder as are necessary or desirable and are not contrary to or inconsistent with the Trust Agreement,

(c) if, in the opinion of Counsel, such amendment, alteration or modification does not materially adversely affect the rights of the Owners of the Bonds,

(d) as may be necessary in connection with the issuance of Additional Bonds pursuant to the provisions of this Trust Agreement, or

(e) with the written consent of the owners of a majority in aggregate principal amount of the Bonds then outstanding and affected by such amendment, alteration or modification, exclusive of issuer-owned Bonds.

Any such written consent shall be obtained in the manner provided in Article VIII hereof for amendments to the Trust Agreement. No such amendment, alteration or modification shall be effective unless and until there shall have been filed with the Trustee an Opinion of Counsel stating that such amendment, alteration or modification has been duly and lawfully entered into by the parties thereto, is authorized or permitted by this Trust Agreement and is valid and binding upon the parties thereto in accordance with its terms. For purposes of this Trust Agreement, no change or revision to Exhibit A of the Installment Sale Agreement and no change or revision of Exhibit B of the Installment Sale Agreement in the manner set forth in such Exhibit B (*i.e.*, upon opinion of Bond Counsel to the effect that such change would not adversely affect the Tax-exempt status of the Bonds) shall constitute an amendment, alteration or modification of the Installment Sale Agreement.

Section 7.07 Further Assurances. The Authority covenants that it shall promptly execute and deliver or cause to be executed and delivered all other and further assurances, documents or instruments and promptly do or cause to be done all such other and further things as may be necessary or reasonably required in order to carry out the purposes and intentions of this Trust Agreement and for preserving and protecting the rights and interests of the Owners.

ARTICLE VIII

AMENDMENTS

Section 8.01 Amendment by Consent of Owners. The Trust Agreement and the rights and obligations of the Authority and of the Owners may be amended at any time by a Supplemental Trust Agreement which shall become binding when the written consents of the Owners of at least a majority in aggregate principal amount of the affected Bonds then Outstanding (exclusive of Bonds disqualified as provided in Section 8.03) and, so long as the Bond Insurance Policy is then in full force and effect, the written consent of the Bond Insurer of the affected Bonds, are filed with the Trustee. No such amendment shall (a) extend the maturity of or reduce the interest rate on, or otherwise alter or impair the obligation of the Authority to pay the interest or principal or redemption premium, if any, at the time and place and at the rate and in the currency provided herein of any Bond, without the express written consent of the Owner of such Bond, or (b) permit the creation by the Authority of any mortgage, pledge or lien upon the Revenues superior to or on a parity with the pledge and lien created in the Trust Agreement for the benefit of the Bonds, or (c) reduce the percentage of Bonds required for the written consent to any such amendment, or (d) modify the rights or obligations of the Trustee without its prior written assent thereto.

Section 8.02 Amendment without Consent of Owners. The Trust Agreement and the rights and obligations of the Authority and of the Owners may also be amended at any time, with written notice to the Bond Insurer, by a Supplemental Trust Agreement which shall become binding upon execution, without the consent of any Owners and to the extent permitted by law and only for any one or more of the following purposes:

- (a) To add to the covenants and agreements of the Authority in the Trust Agreement contained, other covenants and agreements thereafter to be observed,

or to surrender any right or power herein reserved to or conferred upon the Authority;

(b) To make such provisions for the purpose of curing any ambiguity, or of curing, correcting or supplementing any defective provision contained in the Trust Agreement, or in regard to questions arising under the Trust Agreement, as the Authority may deem necessary or desirable and not inconsistent with the Trust Agreement, and which shall not materially adversely affect the interest of the Owners;

(c) To provide for the issuance of any Additional Bonds, and to provide the terms and conditions under which such Additional Bonds may be issued, subject to and in accordance with the provisions of Article VI;

(d) To modify, amend or supplement this Trust Agreement in such manner as to permit the qualification hereof under the Trust Indenture Act of 1939, as amended, or any similar federal statute hereafter in effect;

(e) To maintain the exclusion of interest on the Bonds from gross income for federal income tax purposes (except with respect to any Bonds which the Authority certifies to the Trustee are not intended to qualify for such exclusion);

(f) To the extent necessary to obtain a Bond Insurance Policy, to obtain a rating on the Bonds or in connection with satisfying all or a portion of the Reserve Requirement by crediting a letter of credit or Bond Insurance Policy to the Reserve Account; provided that such amendments which shall not materially adversely affect the interests of the Owners of the Bonds; or

(g) For any other purpose that does not materially adversely affect the interests of the Owners.

Section 8.03 Disqualified Bonds. Bonds owned or held by or for the account of the Authority or the City shall not be deemed Outstanding for the purpose of any consent or other action in this Trust Agreement provided for, and shall not be entitled to consent to, or take any other action in this Trust Agreement provided for; provided, however, that for purposes of determining whether the Trustee shall be protected in relying on any such demand, request, direction, consent or waiver, only Bonds which the Trustee knows to be so owned or held will be disregarded.

Section 8.04 Endorsement or Replacement of Bonds after Amendment. After the effective date of any action taken as hereinabove provided, the Authority may determine that the Bonds may bear a notation, by endorsement in form approved by the Authority, as to such action, and in that case upon demand of the Owner of any Bond Outstanding at such effective date and presentation of his Bond for such purpose at the office of the Trustee or at such additional offices as the Trustee may select and designate for that purpose, a suitable notation as to such action shall be made on such Bond. If the Authority shall so determine, new Bonds so modified as, in the opinion of the Authority, shall be necessary to conform to such action shall be prepared and executed, and in that case upon demand of the

Owner of any Bond Outstanding at such effective date such new Bonds shall be exchanged at the office of the Trustee or at such additional offices as the Trustee may select and designate for that purpose, without cost to each Owner, for Bonds then Outstanding, upon surrender of such Outstanding Bonds.

Section 8.05 Opinion of Counsel. The Trustee may conclusively accept an Opinion of Bond Counsel to the Authority that an amendment of the Trust Agreement is in conformity with the provisions of this Article.

ARTICLE IX

THE TRUSTEE

Section 9.01 Appointment; Resignation or Removal. (a) BNY Western Trust Company, a banking corporation organized under the laws of the State of California, having a corporate trust office in Los Angeles, California, is hereby appointed Trustee hereunder for the purpose of receiving all money which the Authority or the City is required to deposit with the Trustee hereunder and under the Installment Sale Agreement and to allocate, use and apply the same as provided herein and therein.

(b) The Trustee may at any time resign by giving written notice to the Authority. Any successor trustee appointed hereunder shall give notice of such appointment to the Owners, which notice shall be mailed to the Owners at their addresses appearing in the registration books in the office of the Trustee. Upon receiving such notice of resignation, the Authority shall promptly appoint a successor Trustee by an instrument in writing. Any resignation or removal of the Trustee and appointment of a successor Trustee shall become effective only upon acceptance of appointment by the successor Trustee. If, within thirty (30) days after notice of the removal or resignation of the Trustee, no successor Trustee shall have been appointed and shall have accepted such appointment, the removed or resigning Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee, which court may thereupon, after such notice, if any, as it may deem proper and prescribe and as may be required by law, appoint a successor Trustee having the qualifications required hereby.

(c) The Authority may at any time, but only prior to an Event of Default or after the curing or waiver of an Event of Default and only upon thirty (30) days written notice, at its sole discretion remove the Trustee initially appointed, and any successor thereto, and may appoint a successor or successors thereto; provided that any such successor shall be a bank, banking institution (state or federal) or trust company with a corporate trust office in California, having a combined capital (exclusive of borrowed capital) and surplus (or whose parent holding company has a combined capital (exclusive of borrowed capital) and surplus) of at least fifty million dollars (\$50,000,000), and subject to supervision or examination by federal or state authority. If such bank, banking institution or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purposes of this section the combined capital and surplus of such bank, banking institution or trust company shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published.

Section 9.02 Duties. The duties and obligations of the Trustee shall be determined solely by the express provisions of this Trust Agreement. The Trustee shall not be liable except for the performance of such duties and obligations as are specifically set forth in this Trust Agreement, and no implied covenants or obligations shall be read into this Trust Agreement against the Trustee. The permissive right of the Trustee to do things enumerated in this Trust Agreement shall not be construed as a duty and it shall not be answerable for other than its negligence or willful misconduct. In case an Event of Default has occurred and is continuing, the Trustee shall exercise such rights and powers vested in it by this Trust Agreement, and use the same degree of care and skill in their exercise, as a prudent person would exercise or use under the circumstances in the conduct of such person's own affairs. The Trustee may execute any of the trusts or powers hereof and perform the duties required of it hereunder by or through its attorneys, agents or receivers.

Section 9.03 Compensation. The Authority shall from time to time, subject to any agreement between the Authority and the Trustee then in force, pay to the Trustee compensation for its services rendered by it in the execution of the trusts hereby created and in the exercise and performance of any of the powers and duties hereunder of the Trustee, which compensation shall not be limited by any provision of law with respect to the compensation of a trustee of an express trust, and the Authority will reimburse the Trustee for all its advances (with interest on such advances at the maximum rate allowed by law) and expenditures, including but not limited to advances to and fees and expenses of independent accountants, counsel (including in-house counsel to the extent not duplicative of other counsel's work) and engineers or other experts employed by it, and reasonably required, in the exercise and performance of its powers and duties hereunder.

Section 9.04 Indemnification. The Authority shall indemnify and save the Trustee, its officers, employees, directors and agents harmless from and against all claims, losses, costs, expenses, liability and damages, including legal fees and expenses, arising out of (a) any breach of default on the part of the Authority in the performance of any of its obligations under this Trust Agreement, the Installment Sale Agreement, and any related agreements or instruments and any other agreement, (b) any breach of default on the part of the City in the performance of any of its obligations under the Installment Sale Agreement, and any related agreements or instruments and any other agreement, (c) any act or omission of the City or of any of its agents, assignees or licensees with respect to the 2004 Projects or the Water System, (d) the exercise and performance by the Trustee of any of its powers and duties hereunder, so long as such exercise and performance are permitted by and in compliance with the provisions hereof, or (e) the offering and sale of the Bonds or the distribution of any official statement or other offering circular utilized in connection with the sale of the Bonds; provided, that the Authority shall not be liable for actions caused by the Trustee's own negligence or willful misconduct or the negligence or willful misconduct of the Trustee's officers or agents. The Trustee's rights to indemnification and protection from liability hereunder and its rights to payment of its fees and expenses shall survive its resignation or removal and final payment or defeasance of the Bonds. The Trustee shall not be liable for the sufficiency of Revenues or other moneys required to be paid to it under the Trust Agreement (except as provided in this Trust Agreement), or its right to receive moneys pursuant to the Trust Agreement.

Section 9.05 Liability of Trustee. (a) The recitals of facts, covenants and agreements contained herein, in the Bonds and in any instruments of further assurance shall be taken as statements, covenants and agreements of the Authority or the City, as applicable, and the Trustee does not assume any responsibility for the correctness of the same, or make any representation as to the validity or sufficiency of the Trust Agreement or of the Bonds, the adequacy of any security afforded thereunder, or the correctness or completeness of any information contained in any offering materials distributed in connection with the sale of the Bonds, or incur any responsibility in respect of any of the foregoing, other than in connection with the duties or obligations herein or in the Bonds assigned to or imposed upon it. The Trustee shall not be liable in connection with the performance of its duties hereunder, except for its own negligence or willful misconduct.

(b) The Trustee shall not be responsible for the validity, genuineness or performance of any leases, contracts or other instruments at any time conveyed, mortgaged, hypothecated, pledged, assigned or transferred to it hereunder, or with respect to the obligation of the Authority to preserve and keep unimpaired the rights of the Authority under or concerning any such leases, contracts or other instruments. The Trustee makes no representations and shall have no responsibility for any official statement or other offering material prepared or distributed with respect to the Bonds. In accepting the trust hereby created, the Trustee acts solely as Trustee for the Owners and not in its individual capacity and all persons, including without limitation the Owners, the Authority and the City, having any claim against the Trustee arising from this Trust Agreement not attributable to the Trustee's negligence or willful misconduct shall look only to the funds and accounts held by the Trustee hereunder for payment except as otherwise specifically provided herein.

(c) The Trustee shall be under no obligation to exercise any of the rights or powers vested in it by this Trust Agreement at the request or direction of any Owner or any Bond Insurer pursuant to this Trust Agreement unless the Trustee shall have received reasonable security or indemnity against the costs, expenses and liabilities which might be incurred by it in compliance with such request or direction.

(d) The Trustee shall have no duty to see to the payment or discharge of any fees, assessment or other charge or any line of any kind owing with respect to the Water System or any part thereof.

(e) In the absence of bad faith on its part, the Trustee may conclusively rely, as to the truth of the statements and the correctness of the opinions expressed therein, upon certificates or opinions furnished to the Trustee and conforming to the requirements of this Trust Agreement.

(f) The Trustee is not accountable for the use by the Authority or the City of funds which the Trustee releases to the Authority or the City or which such party otherwise receives, or to verify compliance by the City with the provisions of Section 6.03 of the Installment Sale Agreement, or for the adequacy or validity of any collateral or security interest securing this Trust Agreement or the Bonds. The Trustee has no obligation to incur individual financial or other liability or risk in performing any duty or in exercising any right hereunder.

(g) Except during the continuance of an Event of Default, the Trustee undertakes to perform such duties and only such duties as are specifically set forth in this Trust Agreement and no implied covenants or obligations shall be read into this Trust Agreement against the Trustee.

(h) The Trustee shall not be deemed to have knowledge of any Event of Default other than a payment default hereunder unless the Trustee shall be specifically notified in writing of such default by the Authority, the City, the Bond Insurer or by the Owners of at least twenty-five percent (25%) in aggregate principal amount of Bonds then Outstanding and all notices or other instruments required by this Trust Agreement to be delivered to the Trustee must, in order to be effective, be delivered at the Corporate Trust Office of the Trustee, and in the absence of such notice so delivered, the Trustee may conclusively assume there is no Event of Default except as aforesaid. The Trustee shall not be bound to ascertain or inquire as to the performance or observance by any other party of any of the terms conditions, covenants or agreements herein or in any of the documents executed in connection with the Bonds. Any action taken or omitted to be taken by the Trustee in good faith pursuant to this Trust Agreement upon the request of authority or consent of any person who at the time of making such request or giving such authority or consent is the Owner of any Bond, shall be conclusive and binding upon all future Owners of the same Bond executed and delivered in exchange therefor or in place thereof.

(i) The Trustee shall not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of any Bond Insurer or the Owners of a majority in aggregate principal amount of the Outstanding Bonds relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred upon the Trustee, under this Trust Agreement.

(j) The Trustee shall not be considered in breach of or in default with respect to any obligations created hereunder, in the event of an enforced delay in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God, or of the public enemy, acts of a government, acts of the other party hereto, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, litigation or arbitration involving a party or others relating to governmental action or inaction pertaining to the Water System, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee; provided, that in the event of any such enforced delay, the Trustee shall notify the Authority in writing within five (5) business days after (i) the occurrence of the event giving rise to such delay, (ii) the Trustee's actual knowledge of the impending enforced delay, or (iii) the Trustee's knowledge of sufficient facts under which a reasonable person would conclude the enforced delay will occur.

(k) The immunities and exceptions from liability of the Trustee as provided herein shall extend to its officers, directors, employees and agents and such immunities and exceptions and its right to payment of its fees and expenses shall survive its resignation or removal and the final payment and defeasance of the Bonds. Under no circumstances shall the

Trustee be liable in its individual capacity for the obligations evidenced by the Bonds. The Trustee, in its individual or any other capacity, may become the Owner of any Bonds or other obligations of any party hereto with the same rights which it would have if not the Trustee and may act as a depository for and permit any of its officers or directors to act as a member of, or in any other capacity with respect to, any committee formed to protect the rights of owners of Bonds, whether or not such committee shall represent the Owners of the majority in aggregate principal amount of the Bonds then Outstanding. Before taking or refraining from any action hereunder at the request or direction of the Owners or the Bond Insurer, the Trustee may require that an indemnity bond satisfactory to the Trustee be furnished to it and be in full force and effect.

Section 9.06 Notice to Trustee. The Trustee shall be protected in acting upon any notice, indenture, request, consent, order, certificate, report, bond, opinion or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties. The Trustee may consult with counsel, who may be counsel to the Authority or the City, with regard to legal questions, and the opinion of such counsel shall be full and complete authorization and protection in respect of any action taken or suffered hereunder in good faith and in accordance therewith.

The Trustee shall not be bound to recognize any person as the Owner of a Bond unless and until such Bond is submitted for inspection, if required, and such person is the registered owner of such Bond as shown on the registration books.

Whenever in the administration of its duties under this Trust Agreement the Trustee shall deem it necessary or desirable that a matter be proven or established prior to taking or suffering any action hereunder, such matter (unless other evidence in respect thereof be herein specifically prescribed) may, in the absence of bad faith on the part of the Trustee, be deemed to be conclusively proved and established by a Written Certificate of the Authority and such certificate shall be full warrant to the Trustee for any action taken or suffered under the provisions of this Trust Agreement upon the faith thereof, but in its discretion the Trustee may, in lieu thereof, accept other evidence of such matter or may require such additional evidence as to it may seem reasonable.

ARTICLE X

DEFEASANCE

Section 10.01 Discharge of Trust Agreement. (a) Any or all of the Outstanding Bonds may be paid in any of the following ways (each may be performed by or on behalf of the Authority):

- (i) payment of the principal of and interest and premium (if any) on such Bonds, as and when the same become due and payable;
- (ii) deposit with the Trustee, an escrow agent, or any other fiduciary, to hold, at or before maturity, money and/or Federal Securities in the necessary amount (as provided

in Section 10.03) to pay or redeem such Bonds; provided, that if such money or securities are deposited with a fiduciary who is not also the Trustee, then the Authority shall notify the Trustee in writing of such an arrangement; or

(iii) delivery to the Trustee, for cancellation by it, all of such Bonds.

Upon the payment of Bonds as provided above, then notwithstanding that any of such Bonds shall not have been surrendered for payment, this Trust Agreement and the pledge of Revenues and other assets made under this Trust Agreement with respect to such Bonds and all covenants, agreements and other obligations of the Authority under this Trust Agreement with respect to such Bonds shall cease, terminate, become void and be completely discharged and satisfied, except for (A) the right of the Trustee to collect any fees or expenses due hereunder and (B) with respect to a deposit made pursuant to clause (ii) above, the obligation of the Trustee to apply moneys and securities so deposited to the payment of the Bonds as set forth herein and right of the Owners to such payment subject to the provisions of Section 10.04. In such event, upon the Written Request of the Authority, the Trustee shall execute and deliver to the Authority all such instruments as may be necessary or desirable to evidence such discharge and satisfaction, and the Trustee shall pay over, transfer, assign or deliver to the Authority all moneys or securities or other property held by it pursuant to this Trust Agreement which are not required for the payment or redemption of any of such Bonds not theretofore surrendered for such payment or redemption.

(b) The Authority may at any time surrender to the Trustee for cancellation by it any Bonds previously issued and delivered, which the Authority may have acquired in any manner whatsoever, and such Bonds, upon such surrender and cancellation, shall be deemed to be paid and retired.

Section 10.02 Notice to Owners. If any money or proceeds of Federal Securities deposited with the Trustee, escrow agent or other fiduciary pursuant to clause (ii) of Section 10.01(a) above are to be applied toward the optional redemption of Outstanding Bonds pursuant to Section 4.01(b), then the Authority shall notify the Trustee in writing as to the Series, the maturity or maturities, and the principal amounts of Bonds to be so redeemed and the date or dates of redemption. The Trustee shall promptly give notice of redemption to the affected Owners in accordance with Section 4.03.

Section 10.03 Deposit of Money or Securities with Trustee. Whenever in the Trust Agreement it is provided or permitted that there be deposited with or held in trust by the Trustee, escrow agent or fiduciary, money or securities in the necessary amount to pay or redeem any Bonds, the money or securities so to be deposited or held may include money or securities held by the Trustee in the funds and accounts established pursuant to this Trust Agreement and shall be:

(a) lawful money of the United States of America in an amount equal to the principal amount of such Bonds and all unpaid interest thereon to maturity, except that, in the case of Bonds which are to redeemed prior to maturity, the amount to be deposited or held shall be the principal amount of such Bonds, the premium (if any) and all unpaid interest thereon to the redemption date; or

(b) Federal Securities, the principal of and interest on which when due will provide money sufficient to pay the principal of and interest and premium (if any) on the Bonds to be paid or redeemed, as such principal, interest and premium become due; provided, that (i) the sufficiency of such Federal Securities shall be evidenced by a written opinion of an Independent Accountant filed with the Authority, the City and the Trustee, (ii) the Trustee shall have been irrevocably instructed (by the terms of this Trust Agreement or in writing by the Authority) to apply such money to the payment of such principal, interest and premium (if any) with respect to such Bonds and (iii) the Authority shall have delivered to the Trustee an opinion of Bond Counsel to the effect that such Bonds have been discharged in accordance with this Trust Agreement (which opinion may rely upon and assume the accuracy of the Independent Accountant's opinion referred to above).

Section 10.04 Unclaimed Funds. Anything in the Trust Agreement to the contrary notwithstanding, any money held by the Trustee in trust for the payment and discharge of any of the Bonds or interest thereon which remain unclaimed for two (2) years after the date when such Bonds or interest thereon have become due and payable, if such money was held by the Trustee at such date, or for two (2) years after the date of deposit of such money if deposited with the Trustee after the said date when such Bonds or interest thereon become due and payable, shall be repaid by the Trustee to the Authority, as its absolute property and free from trust, and the Trustee shall thereupon be released and discharged with respect thereto and the Owners shall look only to the Authority for the payment of such Bonds; provided, however, that before being required to make any such payment to the Authority, the Trustee shall, at the Written Request of the Authority and at the expense of the Authority, cause to be mailed to the registered Owners of such Bonds at their addresses as they appear on the Registration Books a notice that said money remains unclaimed and that, after a date named in said notice, which date shall not be less than thirty (30) days after the date of the mailing of such notice, the balance of such money then unclaimed will be returned to the Authority. Any money held by the Trustee in trust for the payment and discharge of any Bonds shall not bear interest or be otherwise invested from and after such maturity or redemption date.

ARTICLE XI

EVENTS OF DEFAULT AND REMEDIES

NOTWITHSTANDING ANYTHING TO THE CONTRARY IN THIS ARTICLE XI, SO LONG AS THE BOND INSURANCE POLICY REMAINS IN EFFECT AND THE BOND INSURER HAS NOT DEFAULTED WITH RESPECT TO ITS OBLIGATIONS UNDER THE BOND INSURANCE POLICY, ALL PROVISIONS OF THIS ARTICLE XI SHALL BE SUBJECT TO, AND QUALIFIED BY, THE PROVISIONS SET FORTH IN ARTICLE XII HEREOF AND, WITH RESPECT TO ANY SERIES OF ADDITIONAL BONDS, IN THE PROVISIONS SET FORTH IN THE APPLICABLE SUPPLEMENTAL TRUST AGREEMENT, INCLUDING, WITHOUT LIMITATION, THE BOND INSURER'S RIGHT TO CONSENT TO ACCELERATION OF THE BONDS, AND THE BOND INSURER'S RIGHT TO CONSENT TO OR DIRECT CERTAIN TRUSTEE, AUTHORITY, CITY OR OWNER ACTIONS.

Section 11.01 Events of Default. The following events shall be Events of Default hereunder:

(a) Default in the due and punctual payment of the principal of Bonds when and as the same shall become due and payable, whether at maturity as therein expressed, by proceedings for redemption, by acceleration, or otherwise.

(b) Default in the due and punctual payment of any installment of interest on Bonds when and as the same shall become due and payable.

(c) Default by the Authority in the observance of any of the other covenants, agreements or conditions on its part in this Trust Agreement or in the Bonds contained, if such default shall have continued for a period of thirty (30) days after written notice thereof, specifying such default and requiring the same to be remedied, shall have been given to the Authority by the Trustee; provided, however, that if in the reasonable opinion of the Authority the default stated in the notice can be corrected, but not within such thirty (30) day period, such default shall not constitute an Event of Default hereunder if the Authority shall commence to cure such default within such thirty (30) day period and thereafter diligently and in good faith cure such failure in a reasonable period of time.

(d) The occurrence and continuation of an "Event of Default" as defined in and under the Installment Sale Agreement.

Section 11.02 Remedies Upon Event of Default. If any Event of Default shall occur, then, and in each and every such case during the continuance of such Event of Default the Trustee may, and at the written direction of the Owners of not less than a majority in aggregate principal amount of the Bonds at the time Outstanding the Trustee shall, upon notice in writing to the Authority and the City, declare the principal of all of the Bonds then Outstanding, and the interest accrued thereon, to be due and payable immediately, and upon any such declaration the same shall become and shall be immediately due and payable, anything in this Trust Agreement or in the Bonds contained to the contrary notwithstanding.

Any such declaration is subject to the condition that if, at any time after such declaration and before any judgment or decree for the payment of the moneys due shall have been obtained or entered, the Authority or the City shall deposit with the Trustee a sum sufficient to pay all the principal of and installments of interest on the Bonds payment of which is overdue, with interest on such overdue principal at the rate borne by the respective Bonds, and the reasonable fees, charges and expense (including those of its attorneys) of the Trustee, and any and all other Events of Default known to the Trustee (other than in the payment of principal and interest on the Bonds due and payable solely by reason of such declaration) shall have been made good or cured to the satisfaction of the Trustee or provision deemed by the Trustee to be adequate shall have been made therefor, then, and in every such case, the Trustee, may, on behalf of the Owners of all of the Bonds, rescind and annul such declaration and its consequences and waive such Event of Default; but no such rescission and annulment shall extend to or shall affect

any subsequent Event of Default, or shall impair or exhaust any right or power consequent thereon.

Section 11.03 Application of Revenues and Other Funds after Default. If an Event of Default shall occur and be continuing, all Revenues and any other funds then held or thereafter received by the Trustee under any of the provisions of this Trust Agreement shall be applied by the Trustee as follows and in the following order:

(a) To the payment of any expense necessary in the opinion of the Trustee to protect the interests of the Owners of the Bonds and payment of reasonable fees, charges and expenses of the Trustee (including reasonable fees and disbursements of its counsel) incurred in and about the performance of its duties under this Trust Agreement;

(b) To the payment of the principal of and interest then due on the Bonds (upon presentation of the Bonds to be paid, and stamping or otherwise noting thereon of the payment if only partially paid, or surrender thereof if fully paid) in accordance with the provisions of this Trust Agreement, as follows:

First: To the payment to the persons entitled thereto of all installments of interest then due in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full any installment or installments maturing on the same date, then to the payment thereof ratably, according to the amounts due thereon, to the persons entitled thereto, without any discrimination or preference; and

Second: To the payment to the persons entitled hereto of the unpaid principal of any Bonds which shall have become due, whether at maturity or by acceleration or redemption, with interest on the overdue principal at the rate borne by the respective Bonds (to the extent permitted by law), and, if the amount available shall not be sufficient to pay in full all the Bonds, together with such interest, then to the payment thereof ratably, according to the amounts of principal due on such date to the persons entitled thereto, without any discrimination or preference.

Section 11.04 Trustee to Represent Bond Owners. The Trustee is hereby irrevocably appointed (and the successive respective Owners of the Bonds, by taking and holding the same, shall be conclusively deemed to have so appointed the Trustee) as trustee and true and lawful attorney-in-fact of the Owners of the Bonds for the purpose of exercising and prosecuting on their behalf such rights and remedies as may be available to such Owners under the Bonds, this Trust Agreement and applicable provisions of any law. Upon the occurrence and continuance of an Event of Default or other occasion giving rise to a right in the Trustee to represent the Bond Owners, the Trustee in its discretion may, and upon the written request of the Owners of a majority in aggregate principal amount of the Bonds then Outstanding, and upon being indemnified to its satisfaction therefor, shall, proceed to protect or enforce its rights or the rights of such Owners by such appropriate action, suit, mandamus or other proceedings as it shall deem most effectual to protect and enforce any such right, at law or in equity, either for the

specific performance of any covenant or agreement contained herein, or in aid of the execution of any power herein granted, or for the enforcement of any other appropriate legal or equitable right or remedy vested in the Trustee or in such Owners under the Bonds, this Trust Agreement or any other law; and upon instituting such proceeding, the Trustee shall be entitled, as a matter of right, to the appointment of a receiver of the Revenues and other assets pledged under this Trust Agreement, pending such proceeding. All rights of action under this Trust Agreement or the Bonds or otherwise may be prosecuted and enforced by the Trustee without the possession of any of the Bonds or the production thereof in any proceeding relating thereto, and any such suit, action or proceeding instituted by the Trustee shall be brought in the name of the Trustee for the benefit and protection of all the Owners of such Bonds, subject to the provisions of this Trust Agreement.

Section 11.05 Bond Owners' Direction of Proceedings. The Owners of a majority in aggregate principal amount of the Bonds then Outstanding shall have the right, by an instrument or concurrent instruments in writing executed and delivered to the Trustee, and upon indemnification of the Trustee to its reasonable satisfaction, to direct the method of conducting all remedial proceedings taken by the Trustee hereunder, provided that such direction shall not be otherwise than in accordance with law and the provisions of this Trust Agreement, and that the Trustee shall have the right to decline to follow any such directions which in the opinion of the Trustee would expose it to liability.

Section 11.06 Limitation of Bond Owners' Right to Sue. Notwithstanding any other provision hereof, no Owner of any Bonds shall have the right to institute any suit, action or proceeding at law or in equity, for the protection or enforcement or any right or remedy under this Trust Agreement, the Installment Sale Agreement or any other applicable law with respect to such Bonds, unless (a) such Owner shall have given to the Trustee written notice of the occurrence of an Event of Default; (b) the Owners of a majority in aggregate principal amount of the Bonds then Outstanding shall have made written request upon the Trustee to exercise the powers hereinbefore granted or to institute such suit, action or proceeding in its own name; (c) such Owner or Owners shall have tendered to the Trustee reasonable indemnity against the costs, expenses and liabilities to be incurred in compliance with such request; (d) the Trustee shall have failed to comply with such request for a period of sixty (60) days after such written request shall have been received by, and said tender of indemnity shall have been made to, the Trustee; and (e) no direction inconsistent with such written request shall have been given to the Trustee during such sixty (60) day period by the Owners of a majority in aggregate principal amount of the Bonds then Outstanding.

Such notification, request, tender of indemnity and refusal or omission are hereby declared, in every case, to be conditions precedent to the exercise by any Owner of Bonds of any remedy hereunder or under law; it being understood and intended that no one or more Owners of Bonds shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of this Trust Agreement or the rights of any other Owners of Bonds, or to enforce any right under the Bonds, this Trust Agreement, the Installment Sale Agreement or other applicable law with respect to the Bonds, except in the manner herein provided, and that all proceedings at law or in equity to enforce any such right shall be instituted, had and maintained in the manner herein provided and for the benefit and protection of all Owners of the Outstanding Bonds, subject to the provisions of this Trust Agreement.

Section 11.07 Absolute Obligation of Authority. Nothing in any other provision of this Trust Agreement or in the Bonds contained shall affect or impair the obligation of the Authority, which is absolute and unconditional, to pay the principal of and interest and premium (if any) on the Bonds to the respective Owners of the Bonds at their respective dates of maturity, or upon call for redemption, as herein provided, but only out of the Revenues and other assets herein pledged therefor, or affect or impair the right of such Owners, which is also absolute and unconditional, to enforce such payment by virtue of the contract embodied in the Bonds.

Section 11.08 Termination of Proceedings. In case any proceedings taken by the Trustee or any one or more Bond Owners on account of any Event of Default shall have been discontinued or abandoned for any reason or shall have been determined adversely to the Trustee or the Bond Owners, then in every such case the Authority, the Trustee and the Bond Owners, subject to any determination in such proceedings, shall be restored to their former positions and rights hereunder, severally and respectively, and all rights, remedies, powers and duties of the Authority, the Trustee and the Bond Owners shall continue as though no such proceedings had been taken.

Section 11.09 Remedies Not Exclusive. No remedy herein conferred upon or reserved to the Trustee or to the Owners of the Bonds is intended to be exclusive of any other remedy or remedies, and each and every such remedy, to the extent permitted by law, shall be cumulative and in addition to any other remedy given hereunder or now or hereafter existing at law or in equity or otherwise.

Section 11.10 No Waiver of Default. No waiver of any Event of Default which shall have occurred hereunder, or of any event which with the passage of time if not cured would constitute an Event of Default hereunder, shall be effective without the prior written consent of the Bond Insurer. No delay or omission of the Trustee or of any Owner of the Bonds to exercise any right or power arising upon the occurrence of any Event of Default shall impair any such right or power or shall be construed to be a waiver of any such Event of Default or an acquiescence therein; and every power and remedy given by this Trust Agreement to the Trustee or the Owners of the Bonds may be exercised from time to time and as often as may be deemed expedient.

ARTICLE XII

BOND INSURANCE

Section 12.01 Payments Under the Bond Insurance Policy for Series Bonds. So long as the Bond Insurance Policy for the Series 2004 Bonds are in full force and effect (and the Bond Insurer has not defaulted with respect to its payment obligations thereunder), the following provisions of this Section 12.01 shall apply to and shall govern with respect to the Series 2004 Bonds. All references to the "Bond Insurer" in this Section 12.01 shall mean the Bond Insurer for the Series 2004 Bonds. All references to the "Bond Insurance Policy" in this Section 12.01 shall mean the Bond Insurance Policy for the Series 2004 Bonds.

[to come]

Section 12.02 Notices to Bond Insurer. As long as the Bond Insurance Policy is in full force and effect, any notice that is required to be given to an Owner or to the Trustee pursuant to this Indenture shall also be provided to the Bond Insurer. All notices required to be given to the Bond Insurer under this Trust Agreement shall be in writing and shall be sent by registered or certified mail. All notices to the Bond Insurer for the Series 2004 Bonds shall be sent to _____, _____, Attention: _____

Section 12.03 Control of Remedies upon Default. Notwithstanding the provisions of Article XI, as long as the Bond Insurance Policy is in full force and effect, upon the occurrence and continuance of an Event of Default, the Bond Insurer shall be entitled to control and direct the enforcement of all rights and remedies granted to the Owners of Bonds insured by such Bond Insurer or the Trustee for the benefit of such Owners under this Trust Agreement; provided, however, the Trustee shall not be liable for any action or inaction taken at the direction of the Bond Insurer. Any acceleration of the Bonds or annulment thereof pursuant to Article XI shall be subject to the prior written consent of the Bond Insurer. No waiver of a default with respect to insured Bonds shall be effective without the written consent of the Bond Insurer.

ARTICLE XIII

MISCELLANEOUS

Section 13.01 Benefits of this Trust Agreement. Nothing contained herein, expressed or implied, is intended to give to any person other than the Authority, the Trustee, the City, the Bond Insurer (if any), and the Owners any right, remedy or claim under or by reason hereof. Any agreement or covenant required herein to be performed by or on behalf of the Authority or any officer, employee or agent thereof shall be for the sole and exclusive benefit of the Trustee, the City, the Bond Insurer (if any), and the Owners.

Section 13.02 Execution of Documents by Owners. Any declaration, request or other instrument which is permitted or required herein to be executed by Owners may be in one or more instruments of similar tenor and may be executed by Owners in person or by their attorneys appointed in writing. The fact and date of the execution by any Owner or such Owner's attorney of any declaration, request or other instrument or of any writing appointing such attorney may be proved by the certificate of any notary public or other officer authorized to make acknowledgments of deeds to be recorded in the state or territory in which such Owner purports to act that the person signing such declaration, request or other instrument or writing acknowledged to him the execution thereof, or by an affidavit of a witness of such execution duly-sworn to before such notary public or other officer. The ownership of any Bond and the amount, number and date of holding the same may be proved by the Registration Books. Any declaration, request or other instrument or writing of the Owner of any Bond shall bind all future Owners of such Bond with respect to anything done or suffered to be done by the Authority or the Trustee in good faith and in accordance therewith.

Section 13.03 Severability of Invalid Provisions. If any one or more of the covenants or agreements provided in this Trust Agreement on the part of the Authority to be performed should be contrary to law, then such covenant or covenants or agreement or agreements shall be deemed severable from the remaining covenants and agreements, and shall in no way affect the validity of the other provisions of this Trust Agreement.

Section 13.04 Waiver of Personal Liability. No officer, employee or agent of the Authority shall be individually or personally liable for the payment of principal of, or interest or redemption premiums, if any, on the Bonds by reason of their delivery, but nothing herein contained shall relieve any such officer, employee or agent from the performance of any official duty provided by applicable provisions of law or hereby.

Section 13.05 Notices. Any notice, request, demand or other communication under this Trust Agreement shall be given by first class mail or personal delivery to the party entitled thereto at its address set forth below, or by telecopy or other form of telecommunication, with prompt telephone confirmation. Notice shall be effective either (a) upon transmission by telecopy or other form of telecommunication, (b) upon receipt after deposit in the United States mail, postage prepaid, or (c) in the case of personal delivery to any person, upon actual receipt. The Authority or the Trustee may, by written notice to the other party, from time to time modify the address or number to which communications are to be given hereunder.

If to the Authority:

Morgan Hill Financing Authority
17555 Peak Avenue
Morgan Hill, California 95037
Attention: Treasurer
Fax: (408) 779-3117

If to the City:

City of Morgan Hill
17555 Peak Avenue
Morgan Hill, California 95037
Attention: Director of Finance
Fax: (408) 779-3117

If to the Trustee:

BNY Western Trust Company
700 S. Flower Street, Suite 500
Los Angeles, CA 90017
Attention: Corporate Trust
Fax: (213) 630-6210

Notices to the Bond Insurer for the Series 2004 Bonds shall be governed by Section 12.02.

Any of the foregoing persons may, by notice given under this Section, designate any further or different addresses, telephone numbers or fax numbers to which subsequent notices, certificates, requests or other communications shall be directed.

The Trustee agrees to accept and act upon facsimile transmission of written instructions and/or directions pursuant to the Trust Agreement; provided, however, that: (i) subsequent to such facsimile transmission of written instructions, there shall be provided to the Trustee originally executed instructions and/or directions in a timely manner, (ii) such originally executed instructions and/or directions by the Authority or the City shall be signed by an authorized officer of the Authority or the City or a person designated and authorized to sign for the Authority or the City by an authorized officer of the Authority or the City, as the case may be, and, (iii) each of the Authority and the City shall (A) provide to the Trustee an incumbency certificate listing such designated persons and (B) from time to time provide the Trustee updated incumbency certificates, as necessary or appropriate, reflecting persons who have been added or deleted from the listing.

Section 13.06 CUSIP Numbers. Neither the Authority nor the Trustee shall be liable for any defect or inaccuracy in the CUSIP number that appears on any Bond or in any redemption notice relating thereto. The Trustee may, in its discretion, include in any redemption notice relating to any of the Bonds a statement to the effect that the CUSIP numbers on the Bonds have been assigned by an independent service and are included in such notice solely for the convenience of the Owners and that neither the Authority nor the Trustee shall be liable for any defects or inaccuracies in such numbers.

Section 13.07 Accounts and Funds; Business Days. Any account or fund required herein to be established and maintained by the Trustee may be established and maintained in the accounting records of the Trustee either as an account or a fund, and may, for the purposes of such accounting records, any audits thereof and any reports or statements with respect thereto, be treated either as an account or a fund; but all such records with respect to all such accounts and funds shall at all times be maintained in accordance with this Trust Agreement and sound corporate trust industry practice and with due regard for the protection of the security of the Bonds and the rights of the Owners. Any action required to occur hereunder on a day which is not a Business Day shall be required to occur on the next succeeding Business Day with the same effect as if made on such non-Business Day.

Section 13.08 California Law. This Trust Agreement shall be construed and governed in accordance with the laws of the State.

Section 13.09 Binding on Successors. This Trust Agreement shall be binding upon and inure to the benefit of the parties and their respective successors and assigns.

Section 13.10 Execution in Counterparts. This Trust Agreement may be executed in several counterparts, each of which shall be deemed an original, and all of which shall constitute but one and the same instrument.

Section 13.11 Consent of Parties. Whenever the consent or approval of any party to this Trust Agreement is required by the terms of this Trust Agreement, the consent or approval of such party shall not be unreasonably withheld.

[Remainder of Page Intentionally Left Blank]

IN WITNESS WHEREOF, the parties have executed and attested this Trust Agreement by their officers thereunto duly authorized as of the date and year first written above.

**MORGAN HILL FINANCING
AUTHORITY**

By: _____
Chief Administrative Officer

BNY WESTERN TRUST COMPANY,
as Trustee

By: _____
Authorized Officer

Exhibit A
[Form of Series 2004 Bond]

[UNLESS THIS CERTIFICATE IS PRESENTED BY AN AUTHORIZED REPRESENTATIVE OF THE DEPOSITORY TRUST COMPANY, A NEW YORK CORPORATION (“DTC”), TO THE AUTHORITY OR ITS AGENT FOR REGISTRATION OF TRANSFER, EXCHANGE, OR PAYMENT, AND ANY CERTIFICATE ISSUED IS REGISTERED IN THE NAME OF CEDE & CO. OR IN SUCH OTHER NAME AS IS REQUESTED BY AN AUTHORIZED REPRESENTATIVE OF DTC (AND ANY PAYMENT IS MADE TO CEDE & CO. OR TO SUCH OTHER ENTITY AS IS REQUESTED BY AN AUTHORIZED REPRESENTATIVE OF DTC), ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF, CEDE & CO., HAS AN INTEREST HEREIN.]

No. _____

\$ _____

UNITED STATES OF AMERICA
STATE OF CALIFORNIA

MORGAN HILL FINANCING AUTHORITY
WATER REVENUE BOND
SERIES 2004

INTEREST RATE:	MATURITY DATE:	ORIGINAL DATED DATE:	CUSIP:
	June 1, 20__	_____, 2004	

REGISTERED OWNER: CEDE & CO.

PRINCIPAL AMOUNT: _____ DOLLARS

The MORGAN HILL FINANCING AUTHORITY, a public body corporate and politic, duly organized and existing under the laws of the State of California (the “Authority”), for value received, hereby promises to pay to the Registered Owner specified above or registered assigns (the “Registered Owner”), on the Maturity Date specified above (subject to any right of prior redemption hereinafter provided for), the principal amount specified above, in lawful money of the United States of America, and to pay interest thereon in like lawful money from the Interest Payment Date (as hereinafter defined) next preceding the date of authentication of this Bond unless (i) this Bond is authenticated on or before an Interest Payment Date and after the close of business on the fifteenth day of the month preceding such Interest Payment Date (the “Record Date”), in which event it shall bear interest from such Interest Payment Date, or (ii) this Bond is authenticated on or before the first Record Date preceding the first Interest Payment Date, in which event it shall bear interest from the Original Dated Date specified above;

provided, however, that if at the time of authentication of this Bond, interest has previously been paid or made available for payment on this Bond, at the Interest Rate per annum specified above, payable semiannually on June 1 and December 1 in each year, commencing June 1, 2005 (collectively the "Interest Payment Dates"), calculated on the basis of a 360-day year composed of twelve 30-day months. Principal hereof and premium, if any, upon early redemption hereof are payable upon presentation and surrender hereof at the principal corporate trust office (the "Office") of BNY Western Trust Company, as Trustee (the "Trustee"), in Los Angeles, California, or at such other office as the Trustee may designate. Interest hereon is payable by check of the Trustee mailed by first class mail on the Interest Payment Date to the Registered Owner hereof at the Registered Owner's address as it appears on the registration books of the Trustee as of the close of business on the fifteenth day of the month preceding each Interest Payment Date (a "Record Date"); provided, however, that payment of interest may be by wire transfer in immediately available funds to an account in the United States of America to any Registered Owner of Bonds in the aggregate principal amount of \$1,000,000 or more who shall furnish written wire instructions to the Trustee at least five (5) days before the applicable Record Date.

This Bond is not a debt of the City of Morgan Hill, the County of San Joaquin, the State of California, or any of its political subdivisions, and neither the City, said County, said State, nor any of its political subdivisions, is liable hereon nor in any event shall this Bond be payable out of any funds or properties of the Authority other than the Revenues.

This Bond is one of a duly authorized issue of bonds of the Authority designated as the "Morgan Hill Financing Authority Water Revenue Bonds, Series 2004" (the "Bonds"), in an aggregate principal amount of _____ **Dollars (\$_____)**, all of like tenor and date (except for such variation, if any, as may be required to designate varying numbers, maturities, interest rates or redemption provisions) and all issued pursuant to the provisions of Article 4 of Chapter 5 of Division 7 of Title 1 (commencing with Section 6584) of the Government Code of the State of California (the "Bond Law"), and pursuant to a Trust Agreement, dated as of October 1, 2004, by and between the Authority and the Trustee (the "Trust Agreement"). Subject to certain conditions prescribed in the Trust Agreement, the Authority may issue additional bonds on parity with the Series 2004 Bonds. Reference is hereby made to the Trust Agreement (copies of which are on file at the office of the Authority) and all supplements thereto for a description of the terms on which the Bonds are issued, the provisions with regard to the nature and extent of the Revenues, and the rights thereunder of the owners of the Bonds and the rights, duties and immunities of the Trustee and the rights and obligations of the Authority thereunder, to all of the provisions of which the Registered Owner of this Bond, by acceptance hereof, assents and agrees.

The Series 2004 Bonds have been issued by the Authority to finance certain additions, improvements and betterment to the Water System of the City. In furtherance of the financing the City and the Authority have entered into an Installment Sale Agreement, dated as of October 1, 2004 (the "Installment Sale Agreement"), pursuant to which the City has agreed to purchase certain Facilities (as defined in the Installment Sale Agreement) and make installment payments (the "Installment Payments") as the purchase price therefor which have been calculated to be sufficient to enable the Authority to pay the principal of, and interest and premium (if any) on, the Series 2004 Bonds when due and payable.

This Bond and the interest and premium, if any, hereon and all other Series 2004 Bonds and the interest and premium, if any, thereon (to the extent set forth in the Trust Agreement) are special obligations of the Authority, and are payable from, and secured by a charge and lien on the Revenues as defined in the Trust Agreement, consisting primarily of the Installment Payments. As and to the extent set forth in the Trust Agreement, all of the Revenues are exclusively and irrevocably pledged in accordance with the terms hereof and the provision of the Trust Agreement, to the payment of the principal of and interest and premium (if any) on the Bonds.

The rights and obligations of the Authority and the owners of the Bonds may be modified or amended at any time in the manner, to the extent and upon the terms provided in the Trust Agreement, by no such modification or amendment shall extend to fixed maturity of the Bonds, or reduce the amount of principal thereof or premium (if any) thereon, or extend the time of payment, or change the method of computing the rate of interest thereon, or extend the time of payment of interest thereon, without the consent of the owner of each Bond so affected.

The Bonds maturing on or before June 1, 20[14] are not subject to optional redemption prior to their stated maturity. Bonds maturing on and after June 1, 20[15], are subject to redemption at the option of the Authority as a whole or in part on any Interest Payment Date on or after June 1, 20[14] from any available source of funds at a redemption price equal to 100 percent of the principal amount of the Bonds to be redeemed, together with accrued interest thereon to the date fixed for redemption, with no redemption premium.

As provided in the Trust Agreement, notice of redemption shall be mailed by the Trustee by first class mail not less than thirty (30) nor more than sixty (60) days prior to the redemption date to the respective owners of any Bonds designated for redemption at their address appearing on the registration books of the Trustee, but neither failure to receive such notice nor any defect in the notice so mailed shall affect the sufficiency of the proceedings for redemption or the cessation of accrual of interest thereon from and after the date fixed for redemption.

If this Bond is called for redemption and payment is duly provided therefor as specified in the Trust Agreement, interest shall cease to accrue hereon from and after the date fixed for redemption.

If an Event of Default, as defined in the Trust Agreement, shall occur, the principal of all Bonds may be declared due and payable upon the conditions, in the manner and with the effect provided in the Trust Agreement, but such declaration and its consequences may be rescinded and annulled as further provided in the Trust Agreement.

This Bond is transferable by the Registered Owner hereof, in person or by his attorney duly authorized in writing, at the Office of the Trustee, but only in the manner, subject to the limitations and upon payment of the charges provided in the Trust Agreement, and upon surrender and cancellation of this Bond. Upon registration of such transfer, a new Bond or Bonds, of authorized denomination or denominations, for the same aggregate principal amount and of the same maturity will be issued to the transferee in exchange herefor. This Bond may be

exchanged at the Office of the Trustee for Bonds of the same tenor, aggregate principal amount, interest rate and maturity, of other authorized denominations.

The Authority and the Trustee may treat the Registered Owner hereof as the absolute owner hereof for all purposes, and the Authority and the Trustee shall not be affected by any notice to the contrary.

It is hereby certified that all of the things, conditions and acts required to exist, to have happened or to have been performed precedent to and in the issuance of this Bond do exist, have happened or to have been performed in due and regular time, form and manner as required by the Bond Law and the laws of the State of California and that the amount of this Bond, together with all other indebtedness of the Authority, does not exceed any limit prescribed by the Bond Law or any laws of the State of California, and is not in excess of the amount of Bonds permitted to be issued under the Trust Agreement.

This Bond shall not be entitled to any benefit under the Trust Agreement or become valid or obligatory for any purpose until the certificate of authentication hereon endorsed shall have been signed manually by the Trustee.

IN WITNESS WHEREOF, the Morgan Hill Financing Authority has caused this Bond to be executed in its name and on its behalf with the manual or facsimile signature of its President and attested to by the manual or facsimile signature of its Secretary, all as of the dated date of the Bonds.

MORGAN HILL FINANCING AUTHORITY

By: _____
President

Attest:

Secretary

=====

STATEMENT OF INSURANCE

[to come]

=====

[TRUSTEE'S CERTIFICATE OF AUTHENTICATION]

This is one of the Bonds described in the within-mentioned Trust Agreement.

Date:

BNY WESTERN TRUST COMPANY,
as Trustee

By: _____
Authorized Signatory

=====

(FORM OF ASSIGNMENT)

For value received, the undersigned do(es) hereby sell, assign and transfer unto

(Name, Address and Tax Identification or Social Security
Number of Assignee)

the within Bond and do(es) hereby irrevocably constitute and appoint _____, attorney, to transfer the same on the registration books of the Trustee, with full power of substitution in the premises.

Dated:

Signature Guaranteed:

NOTICE: Signature(s) must be guaranteed by an eligible guarantor institution.

NOTICE: The signature on this assignment must correspond with the name(s) as written on the any face of the within Bond in every particular without alteration or enlargement or any change whatsoever.

NEW ISSUE – BOOK ENTRY ONLY

RATINGS (____ Insured) : S&P: “____”
 Moody’s: “____”
 (See “RATINGS”)

herein.)

In the opinion of Richards, Watson & Gershon, A Professional Corporation, Los Angeles, California, Bond Counsel, based on existing law and assuming compliance with certain covenants set forth in the documents pertaining to the Bonds and requirements of the Internal Revenue Code of 1986, as amended (the “Code”), as described herein, interest on the Bonds is not included in gross income of the owners thereof for federal income tax purposes. In the opinion of Bond Counsel, interest on the Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation’s alternative minimum tax and environmental tax liabilities. In the further opinion of Bond Counsel, interest on the Bonds is exempt from personal income taxes imposed by the State of California. See “TAX MATTERS” herein.

\$ _____ *

MORGAN HILL FINANCING AUTHORITY
WATER REVENUE BONDS
SERIES 2004

Dated: Date of Delivery

Due: June 1, as shown on the inside front cover

The Morgan Hill Financing Authority (the “Authority”) will issue its Water Revenue Bonds, Series 2004 (the “Bonds”) under a Trust Agreement, dated as of October 1, 2004 (the “Trust Agreement”), by and between the Authority and BNY Western Trust Company, as Trustee. Proceeds from the sale of the Bonds will be used to (i) provide funds to the City of Morgan Hill (the “City”) to finance certain capital improvements to the City’s water system (the “Water System”), (ii) fund a reserve account for the Bonds, and (iii) pay certain costs of issuance of the Bonds.

The Bonds will be payable solely from and secured by Revenues and certain funds and accounts held under the Trust Agreement. Revenues consist primarily of certain installment payments (“Installment Payments”) to be made by the City pursuant to an Installment Sale Agreement, dated as of October 1, 2004 (the “Installment Sale Agreement”), by and between the City and the Authority. The Installment Payments are special limited obligations of the City payable solely from and secured by a pledge of and first lien on Net Revenues. Net Revenues consist of certain revenues of the Water System as more fully described herein. The City’s obligation to pay the Installment Payments is ranked on a parity with certain outstanding indebtedness of the City and is subordinate to the City’s obligation with respect to installment payments payable under that certain Installment Payment Agreement, dated as of May 1, 1999, by and between the City and the Morgan Hill Wastewater Facilities Financing Corporation relating to the outstanding Refunding Certificates of Participation (Water System Improvement Projects) Series 1999. See “SECURITY FOR THE BONDS” herein.

The Bonds are subject to optional redemption and mandatory sinking account redemption prior to maturity as described herein.

The Bonds will be issued in fully registered form and, when issued, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York (“DTC”). DTC will act as securities depository of the Bonds. Individual purchases of the Bonds may be made in book-entry form only, in denominations of \$5,000 each or any integral multiple thereof. Purchasers will not receive certificates representing their interest in the Bonds purchased. Principal of and interest on the Bonds will be paid directly to DTC by the Trustee. Principal of the Bonds is payable on their maturity dates set forth on the inside cover hereof. Interest on the Bonds is payable on June 1 and December 1 of each year, commencing June 1, 2005. Upon its receipt of payments of principal and interest, DTC is in turn obligated to remit such principal and interest to DTC participants for subsequent disbursement to the beneficial owners of the Bonds as described herein. See “THE BONDS – Book-Entry Only System” and “APPENDIX F – DTC’S BOOK-ENTRY ONLY SYSTEM” herein.

THE BONDS ARE LIMITED OBLIGATIONS OF THE AUTHORITY PAYABLE SOLELY FROM, AND SECURED BY A PLEDGE OF, REVENUES AND CERTAIN FUNDS AND ACCOUNTS HELD UNDER THE TRUST AGREEMENT. THE AUTHORITY HAS NO TAXING POWER. THE CITY’S OBLIGATION TO PAY INSTALLMENT PAYMENTS IS A SPECIAL OBLIGATION OF THE CITY LIMITED SOLELY TO THE NET REVENUES. NO OTHER FUNDS OR PROPERTY OF THE CITY ARE LIABLE FOR THE PAYMENT OF THE INSTALLMENT PAYMENTS OR ANY OTHER AMOUNTS PAYABLE UNDER THE INSTALLMENT SALE AGREEMENT OR THE TRUST AGREEMENT. NEITHER THE BONDS NOR THE OBLIGATION OF THE CITY TO MAKE INSTALLMENT PAYMENTS CONSTITUTES AN INDEBTEDNESS OF THE AUTHORITY, THE CITY, THE STATE OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL DEBT LIMITATION.

Scheduled payment of the principal of and interest on the Bonds will be insured by a financial guaranty insurance policy to be issued by _____ simultaneously with the delivery of the Bonds.

[BOND INSURER LOGO]

See the section of this Official Statement entitled “BONDOWNERS’ RISKS” for a discussion of certain of the risk factors that should be considered, in addition to other matters set forth herein, in evaluating the investment quality of the Bonds. This cover page contains information for quick reference only. It is not a summary of this issue. Potential purchasers must read the entire Official Statement to obtain information essential to making an informed investment decision.

The Bonds will be sold by competitive sale, expected to be held on October 19, 2004.* See “Appendix H – Form of Official Notice Inviting Bids” herein.

This Preliminary Official Statement and the information contained herein are subject to completion or amendment. These securities may not be sold nor may offers to buy be accepted prior to the time the Official Statement is delivered in final form. Under no circumstances shall this Preliminary Official Statement constitute an offer to sell or a solicitation of an offer to buy nor shall there be any sale of these securities in any jurisdiction in which such offer, solicitation or sale would be unlawful.

The Bonds are offered when, as and if issued, subject to the approval as to their legality by Richards, Watson & Gershon, A Professional Corporation, Los Angeles, California, Bond Counsel. Certain legal matters will also be passed on for the Authority by Richards, Watson & Gershon, as Disclosure Counsel. It is anticipated that the Bonds will be available for delivery in book-entry form through the facilities of DTC on or about _____, 2004.

Dated: _____, 2004

* Preliminary; subject to change.

\$ _____ *

MORGAN HILL FINANCING AUTHORITY
WATER REVENUE BONDS
SERIES 2004

MATURITY SCHEDULE

\$ _____ Serial Bonds

Maturity Date (_____)	Principal Amount	Interest Rate	Yield	CUSIP [†] (_____)	Maturity Date (_____)	Principal Amount	Interest Rate	Yield	CUSIP [†] (_____)
-----------------------------	---------------------	------------------	-------	-------------------------------	-----------------------------	---------------------	------------------	-------	-------------------------------

\$ _____ % Term Bonds due _____, 20__ Yield: ____% CUSIP _____

\$ _____ % Term Bonds due _____, 20__ Yield: ____% CUSIP _____

[†] CUSIP Copyright 2003, American Bankers' Association. CUSIP data herein is provided by Standard & Poor's CUSIP Service Bureau, a division of The McGraw-Hill Companies, Inc. Neither of the Authority nor the City guarantees the accuracy of the CUSIP data.

* Preliminary; subject to change.

No dealer, broker, salesperson or other person has been authorized by the Authority or the City to give any information or to make any representations other than those contained herein. If given or made, such other information or representations must not be relied upon as having been authorized by any of the foregoing. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy any Bonds by any person in any jurisdiction in which such offer of solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful for such person to make such an offer, solicitation or sale. This Official Statement is not to be construed as a contract with the purchasers of the Bonds. Statements contained in this Official Statement which involve estimates, forecasts or matter of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as a representation of fact.

Certain statements included or incorporated by reference in this Official Statement constitute "forward-looking statements." Such statements are generally identifiable by the terminology used such as "plan," "expect," "estimate," "budget," or other similar words and include, but are not limited to, statements under the captions "THE WATER SYSTEM" and "WATER SYSTEM FINANCIAL INFORMATION." The achievement of certain results or other expectations contained in such forward-looking statements involves known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. While the City has agreed to provide certain on-going financial and other data for a limited period of time (see "CONTINUING DISCLOSURE"), neither the Authority nor the City plans to issue any updates or revisions to those forward-looking statements if or when their expectations or events, conditions or circumstances on which such statements are based change.

The information set forth herein has been obtained from the Authority, the City and other sources that are believed to be reliable, but it is not guaranteed as to its accuracy or completeness. The information and expressions of opinions herein are subject to change without notice, and neither delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Authority or the City since the date hereof. All summaries of the resolutions, the Trust Agreement, laws and statutes or other documents are made subject to the provisions of such documents, respectively, and do not purport to be complete statements of any or all of such provisions.

This Official Statement is submitted in connection with the sale of the Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

The Bonds have not been registered under the Securities Act of 1933, as amended, nor has the Trust Agreement been qualified under the Trust Indenture Act of 1939, as amended, in reliance upon an exception from the registration requirements contained in such acts. The Bonds have not been registered or qualified under the securities laws of any state.

IN CONNECTION WITH THE OFFERING OF THE BONDS, THE UNDERWRITER MAY OVER ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SECURITIES OFFERED HEREBY AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

THE UNDERWRITER MAY OFFER AND SELL BONDS TO CERTAIN DEALERS AND OTHERS AT A PRICE LOWER THAN THE OFFERING PRICE. THE OFFERING PRICE MAY BE CHANGED FROM TIME TO TIME BY THE ORIGINAL PURCHASERS.

**CITY OF MORGAN HILL
SANTA CLARA, CALIFORNIA**

CITY COUNCIL

Dennis Kennedy, *Mayor*
Greg Sellers, *Mayor Pro Tem*
Larry Carr, *Council Member*
Hedy L. Chang, *Council Member*
Steve Tate, *Council Member*

CITY OFFICIALS AND STAFF

J. Edward Tewes, *City Manager*
Michael J. Roorda, *City Treasurer*
Jack Dilles, *Director of Finance*
Jim Ashcraft, *Director of Public Works*
Helene Leichter, *City Attorney*
Irma Torrez, *City Clerk*

MORGAN HILL FINANCING AUTHORITY

AUTHORITY COMMISSION

Dennis Kennedy, *President*
Greg Sellers, *Vice President*
Larry Carr, *Member*
Hedy L. Chang, *Member*
Steve Tate, *Member*

SPECIAL SERVICES

Bond Counsel and Disclosure Counsel

Richards, Watson & Gershon,
A Professional Corporation
Los Angeles, California

Financial Advisor

RBC Dain Rauscher Inc.
San Francisco, California

Trustee

BNY Western Trust Company
Los Angeles, California

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§ _____ *

**MORGAN HILL FINANCING AUTHORITY
WATER REVENUE BONDS
SERIES 2004**

INTRODUCTION

This introduction does not purport to be complete, and reference is made to the body of this Official Statement, appendices and the documents referred to herein for more complete information with respect to matters concerning the Bonds. Potential investors are encouraged to read the entire Official Statement. Capitalized terms used and not defined in this Introduction shall have the meanings assigned to them elsewhere in this Official Statement.

General

This Official Statement, including the cover page, inside cover page and appendices hereto, is provided to furnish information in connection with the sale by the Morgan Hill Financing Authority (the “Authority”) of its § _____ * aggregate principal amount Water Revenue Bonds, Series 2004 (the “Bonds”). The Bonds are being issued pursuant to the provisions relating to the joint exercise of powers found in Chapter 5 of Division 7 of Title 1 of the California Government Code, including the provisions of the Marks-Roos Local Bond Pooling Act of 1985, constituting Article 4 thereof (the “Bond Law”), and a Trust Agreement, dated as of October 1, 2004 (the “Trust Agreement”), by and between the Authority and BNY Western Trust Company, as the trustee (the “Trustee”). Proceeds from the sale of the Bonds will be used to (i) provide funds to the City of Morgan Hill (the “City”) to finance certain capital improvements to the City’s water system (the “Water System”), (ii) fund a reserve account for the Bonds, and (iii) pay certain costs of issuance of the Bonds.

The Bonds are payable solely from, and secured by a pledge of, Revenues (defined below) and moneys in certain funds and accounts held under the Trust Agreement. Revenues consist primarily of certain installment payments (“Installment Payments”) to be made by the City to the Authority pursuant to an Installment Sale Agreement, dated as of October 1, 2004 (the “Installment Sale Agreement”), by and between the Authority and the City. The Installment Payments are special limited obligations of the City payable solely from and secured by a pledge of Net Revenues (defined below, see “SECURITY FOR THE BONDS – City’s Pledge of Net Revenues; Water Revenue Fund”) of the Water System. The City’s obligation to pay the Installment Payments out of the revenues of the Water System is ranked on a parity with the loan (the “2003 Loan”) made by the Authority to the City pursuant to a Loan Agreement, dated as of December 1, 2003 (the “2003 Loan Agreement”) and is subordinate to the City’s obligation with respect to installment payments (the “1999 Installment Payments”) relating to the outstanding Refunding Certificates of Participation (Water System Improvement Projects) Series 1999 (the “1999 Certificates”). See “Security for the Bonds” below.

Interest on the Bonds is payable on June 1 and December 1 of each year, commencing June 1, 2005. The Bonds will mature in the amounts and on the dates and bear interest at rates shown on the inside cover of this Official Statement.

The Bonds will be issued in fully registered form only and, when issued and delivered, will be registered in the name of Cede & Co., as nominee of the Depository Trust Company, New York, New

* Preliminary; subject to change.

York (“DTC”). DTC will act as the depository for the Bonds and all payments due on the Bonds will be made to Cede & Co. Ownership interests in the Bonds may be purchased only in book-entry form. See “THE BONDS – Book-Entry Only System” and “APPENDIX F – DTC’S BOOK-ENTRY ONLY SYSTEM.”

The Authority has awarded the Bonds to _____ in a competitive sale held on October 19, 2004.* _____ will act as the original underwriter for the Bonds. See “UNDERWRITING.”

Bond Insurance

Payment of the principal of and interest on the Bonds, when due, will be insured by a municipal bond insurance policy (the “Bond Insurance Policy”) to be issued concurrently with the delivery of the Bonds by _____. See “BOND INSURANCE” and “APPENDIX G – SPECIMEN OF BOND INSURANCE POLICY.”

The City and the Water System

The City is located in Santa Clara County, California (the “County”), against the foothills of the Coastal Ranges near the southern end of the Santa Clara Valley. The City lies about 70 miles south of San Francisco and 20 miles south of San Jose, and sits cradled in a long narrow valley floor between the Santa Cruz Mountains on the west and Mount Hamilton Range on the east. The City has a population of approximately 35,500, as of January 1, 2004. See “APPENDIX A – SUPPLEMENTAL INFORMATION ABOUT THE CITY OF MORGAN HILL” for more information about the City.

The City provides potable water service to its residential and commercial/industrial customers within the City limits and some adjacent unincorporated county areas. The service area of the Water System (the “Service Area”) is approximately six miles across from east to west and five and one-half miles across from north to south. Major Water System facilities currently include 13 groundwater wells (11 of which are active), 10 water storage tanks, 10 booster stations, and over 160 miles of pressured pipes. As of _____, 2004, there were ____ residential accounts and ____ commercial/industrial accounts served by the Water System. See “THE WATER SYSTEM” and WATER SYSTEM FINANCIAL INFORMATION.”

Capital Improvement Program; Plan of Financing

In May 2002, the City Council of the City accepted a report, dated January 9, 2002, prepared by Carollo Engineers, Walnut Creek, California (the “Water System Consultant”), as the updated City of Morgan Hill Water System Master Plan (the “2002 Master Plan”). The Water System Consultant evaluated the Water System’s supply, storage and distribution capacities and provided recommendations on a capital improvement program that is designed to allow the City to meet its projected demands. The recommended improvements include new groundwater wells, storage tanks, booster stations, pipes, casing and pressure reducing valves. Proceeds from the sale of the Bonds are expected to be used to finance the costs of a portion of these recommended improvements. See “PLAN OF FINANCING” and “THE WATER SYSTEM – Demand and Requirement Projections” and “– Capital Improvement Program.”

* Preliminary; subject to change.

Security for the Bonds

The Bonds will be payable solely from and secured by Revenues and certain funds and accounts held under the Trust Agreement. Revenues consist primarily of Installment Payments to be made by the City to the Authority under the Installment Sale Agreement. Pursuant to the Trust Agreement, the Authority has assigned to the Trustee for the benefit of the Owners of the Bonds, certain of its rights under the Installment Sale Agreement, including its rights to receive Installment Payments for the purpose of securing the payment of debt service on the Bonds. The Installment Payments are special limited obligations of the City payable solely from and secured by a pledge of and first lien on Net Revenues of the Water System. The City's obligation to pay the Installment Payments is ranked on a parity with the 2003 Loan and is subordinate to the 1999 Installment Payments. As of September 30, 2004, the remaining outstanding principal amount of the 2003 Loan is \$1,470,437 and the remaining outstanding principal amount of the 1999 Certificates is \$4,360,000.

The City covenants under the Installment Sale Agreement that, at all times while the Bonds remain Outstanding, the City will fix, prescribe, revise and collect rates, fees and charges for the services and facilities furnished by the Water System during each Fiscal Year, so that Gross Revenues less Operation and Maintenance Costs (each as defined below, see "SECURITY FOR THE BONDS – City's Pledge of Net Revenues; Water Revenue Fund") will be equal to at least 120 percent of the aggregate amount payable by the City during such Fiscal Year with respect to the 1999 Installment Payments, the Installment Payments, and any other outstanding obligations which rank on a parity with the Installment Payments.

A Reserve Account will be established and maintained by the Trustee pursuant to the Trust Agreement. Upon issuance of the Bonds, the Trustee will deposit \$_____ * from the sale proceeds of the Bonds into the Reserve Account, which amount is equal to the initial Reserve Requirement (defined below, see "SECURITY FOR THE BONDS – Reserve Account"). Installment Payments payable by the City under the Installment Sale Agreement are calculated to be sufficient to permit the Authority to pay the principal of, and interest on, the Bonds when due. Pursuant to the Trust Agreement, money in the Reserve Account will be used by the Trustee to replenish the Interest Account and/or the Principal Account in the event of deficiency in such accounts for payment of interest and/or principal of the Bonds.

The City's obligation to pay Installment Payments is a special obligation of the City limited solely to the Net Revenues. No other fund or property of the City is liable for the payment of the Installment Payments. Neither the Authority nor the Trustee nor any Owner of the Bonds shall have the right, directly or indirectly, to require or compel the exercise of the ad valorem taxing power of the City or the forfeiture of any property of the City, including the Water System, for the making of any payments under the Installment Sale Agreement or the Trust Agreement.

See "SECURITY FOR THE BONDS" and "BONDOWNERS' RISKS."

Professionals Involved in the Offering

BNY Western Trust Company, Los Angeles, California, will act as Trustee with respect to the Bonds.

RBC Dain Rauscher Inc., San Francisco, California, has served as Financial Advisor to the Authority and the City in connection with the Bonds and has assisted the Authority and the City in structuring the Bonds.

* Preliminary; subject to change.

All proceedings in connection with the issuance of the Bonds are subject to the approval of Richards, Watson & Gershon, A Professional Corporation, Los Angeles, California, Bond Counsel. Certain legal matters will also be passed on for the Authority by Richards, Watson & Gershon, as Disclosure Counsel. The fees and expenses of the Financial Advisor, Bond Counsel, and Disclosure Counsel are contingent upon the sale and delivery of the Bonds.

Continuing Disclosure

The City covenants in a Continuing Disclosure Agreement to prepare and deliver an annual report to certain national and state repositories and to provide certain other information. See “CONTINUING DISCLOSURE” and “APPENDIX E – FORM OF CONTINUING DISCLOSURE AGREEMENT.”

Summaries of Documents

There follows in this Official Statement descriptions of the Bonds, the Trust Agreement, the Installment Sale Agreement, the Authority, the City, the Water System, and various other agreements and documents. The descriptions and summaries of documents herein do not purport to be comprehensive or definitive, and reference is made to each such document for the complete details of all terms and conditions. All statements herein are qualified in their entirety by reference to each such document and, with respect to certain rights and remedies, to laws and principles of equity relating to or affecting creditors’ rights generally. Capitalized terms not defined herein shall have the meanings set forth in the Trust Agreement. Copies of the Trust Agreement and the Installment Sale Agreement are available for inspection during business hours at the corporate trust office of the Trustee in Los Angeles, California.

Other Information

This Official Statement speaks only as of its date as set forth on the cover hereof, and the information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall under any circumstances create any implication that there has been no change in the affairs of the Authority or the City since the date hereof.

Unless otherwise expressly noted, all references to Internet websites in this Official Statement, including without limitation, the City’s website, are shown for reference and convenience only, and none of their content is incorporated herein by reference. The information contained within such websites has not been reviewed by the Authority or the City and neither the Authority nor the City makes no representation regarding the information therein..

PLAN OF FINANCING

The Bonds are being sold by the Authority to assist the City with the financing of certain improvements to the City’s Water System. Proceeds from the sale of the Bonds will be used to finance a portion of the capital improvements (the “Financed Facilities”) recommended by the 2002 Master Plan. The Financed Improvements are expected to include *[more description to come]*.

At the option of the City, the proceeds of the Bonds may be used to finance the costs of other capital additions or improvements to, or replacement of, any part of the Water System, without notice or consent of the owners of Bonds, so long as the City has obtained a bond counsel opinion that such use would not, in and of itself, adversely affect the tax exempt status of the Bonds.

SOURCES AND USES OF FUNDS

The following table shows the estimated sources and uses of the proceeds from the sale of the Bonds:

Sources:

Par amount of the Bonds	\$. *
[Less/Plus]: Original issue [discount/premium]	<u>. </u>
Total Sources	<u><u>\$. </u></u>

Uses:

Project Fund	\$.
Reserve Account	
Costs of Issuance ⁽¹⁾	<u>. </u>
Total Uses	<u><u>\$. </u></u>

(1) Costs of Issuance include underwriter's discount, premium for the Bond Insurance Policy, fees and expenses for Bond Counsel, Disclosure Counsel, Financial Advisor, Trustee, printing expenses and other costs.

* Preliminary; subject to change.

ANNUAL DEBT SERVICE

The following table shows the scheduled annual debt service for the Bonds:

<u>Bond Year Ending June 1</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Annual Debt Service</u>
---	-------------------------	------------------------	---

[to come]

THE BONDS

General

The Bonds will be issued in the aggregate principal amount and will mature on the dates and bear interest at the rates per annum as set forth on the inside front cover of this Official Statement. The Bonds will be issued in authorized denominations of \$5,000 each or integral multiples thereof and will be dated their date of delivery. Interest on the Bonds will be calculated on the basis of a 360-day year of twelve 30-day months and payable on June 1 and December 1 of each year, commencing June 1, 2005 (each an "Interest Payment Date"), until maturity or earlier redemption thereof. The Bonds will be initially delivered as one fully registered certificate for each maturity and will be delivered by means of the book-entry system of DTC. See "Book-Entry Only System" below.

Redemption

Optional Redemption.* The Bonds maturing on or before June 1, 2014 are not subject to optional redemption. The Bonds maturing on or after June 1, 2015 will be subject to redemption by the Authority, as a whole or in part, from proceeds of prepayments made at the option of the City under the Installment Sale Agreement on any date on or after June 1, 2014. The Bonds so called for optional redemption will be redeemed at a redemption price equal to 100 percent of the principal amount of the Bonds to be redeemed, plus accrued interest thereon to the date of redemption, without premium.

Sinking Account Redemption.* The Bonds maturing on June 1, 20__, and the Bonds maturing on June 1, 20__ are subject to redemption in part by lot from sinking account payments made by the Authority, at a redemption price equal to the principal amount thereof to be redeemed with accrued interest thereon to the redemption date, without premium, in the aggregate respective principal amounts and on the respective dates as set forth in the following tables; provided, however, if some but not all of the term Bonds of a maturity have already been optionally redeemed, each future sinking account payment with respect to such term Bonds will be reduced on a pro rata basis (as nearly as practicable) in integral multiples of \$5,000, so that the total amount of sinking account payments with respect to such term Bonds to be made subsequent to an optional redemption shall be reduced in an amount equal to the principal amount of the term Bonds so redeemed, all to be designated pursuant to written notice filed by the Authority with the Trustee:

Term Bonds Maturing on June 1, 20__

<u>Redemption Date</u>	<u>Principal Amount to be Redeemed</u>
------------------------	--

Term Bonds Maturing on June 1, 20__

<u>Redemption Date</u>	<u>Principal Amount to be Redeemed</u>
------------------------	--

* Preliminary; subject to change.

In lieu of a sinking account redemption as described above, the Trustee may apply amounts in the Principal Account to purchase term Bonds at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Account) as may be directed by the Authority, except that the purchase price (exclusive of accrued interest) may not exceed the redemption price then applicable to such Bonds, as set forth in writing by the Authority; provided, however, that no term Bonds shall be purchased by the Trustee with a settlement date more than 60 days prior to the date on which the Authority would otherwise redeem such term Bonds. The principal amount of any term Bonds so purchased by the Trustee will be credited towards and will reduce the Principal Account payment otherwise required to be made with respect to such term Bonds on the applicable redemption date.

Notice of Redemption. Notice of redemption will be sent not less than 30 nor more than 60 days prior to the redemption date, to each of the registered owners of the Bonds designated for redemption at their addresses appearing on the Bond registration books of the Trustee. Such notice shall also be given to the Securities Depositories and to one or more of the Information Services. Neither failure to receive such notice nor any defect in the notice so mailed will affect the sufficiency of the proceedings for the redemption of any Bonds or the cessation of interest thereon on the redemption date.

Selection of Bonds for Redemption. Whenever provision is made in the Trust Agreement for less than all of the Bonds of any maturity to be redeemed, the Trustee will select the Bonds to be redeemed from all Bonds not previously called for redemption, among maturities (unless the maturity or maturities are otherwise specified in the Trust Agreement or by the Authority), and by lot within a maturity, in any manner which the Trustee in its discretion shall deem appropriate. For purposes of such selection, all Bonds will be deemed to be comprised of separate \$5,000 portions and such portions will be treated as separate bonds which may be separately redeemed.

Effect of Redemption. If notice of redemption has been duly given as aforesaid and money for the payment of the redemption price of the Bonds called for redemption has been duly provided, such Bonds so called will cease to be entitled to any benefit under the Trust Agreement other than the right to receive payment of the redemption price, and no interest shall accrue thereon from and after the redemption date specified in such notice.

Book-Entry Only System

The Bonds will be issued as one fully registered bond without coupons for each maturity of each series and, when issued, will be registered in the name of Cede & Co., as nominee of DTC. DTC will act as securities depository of the Bonds. Individual purchases may be made in book-entry form only, in the principal amount of \$5,000 and integral multiples thereof. Purchasers will not receive certificates representing their interest in the Bonds purchased. Principal and interest will be paid to DTC, which will in turn remit such principal and interest to its participants for subsequent disbursement to the beneficial owners of the Bonds as described herein. So long as DTC's book-entry system is in effect with respect to the Bonds, notices to Owners of the Bonds by the Authority or the Trustee will be sent to DTC. Notices and communication by DTC to its participants, and then to the beneficial owners of the Bonds, will be governed by arrangements among them, subject to then effective statutory or regulatory requirements. See "APPENDIX D – DTC'S BOOK-ENTRY ONLY SYSTEM."

In the event that such book-entry system is discontinued with respect to the Bonds, the Authority will execute and deliver replacements in the form of registered certificates and, thereafter, the Bonds will be transferable and exchangeable on the terms and conditions provided in the Trust Agreement. In

addition, the following provisions would then apply: The principal of, and redemption premium, if any, on the Bonds will be payable on the surrender thereof at maturity or the redemption date, as applicable, at the corporate trust office of the Trustee in Los Angeles, California. The interest on the Bonds will be payable by check mailed or draft on each Interest Payment Date to the registered owners thereof as shown on the registration books of the Trustee as of the close of business on the Record Date (*i.e.*, 15th day of the month preceding the Interest Payment Date); provided, that a registered owner of \$1,000,000 or more in aggregate principal amount of Bonds may specify in writing prior to the Record Date that the interest payment payable on each succeeding Interest Payment Date be made by wire transfer.

SECURITY FOR THE BONDS

Pledge of Revenues under Trust Agreement

The Bonds are payable from, and secured by, a pledge of Revenues and certain funds and accounts established and held by the Trustee under the Trust Agreement. Revenues, as defined in the Trust Agreement, means (a) all amounts received by the Authority or the Trustee pursuant to or with respect to the Installment Sale Agreement, including, without limiting the generality of the foregoing, all the Installment Payments (including both timely and delinquent payments, any late charges, and whether paid from any source), prepayments, insurance proceeds, condemnation proceeds, and (b) all interest, profits, or other income derived from the investment of amounts in any fund or account established pursuant to the Trust Agreement.

The Authority will assign to the Trustee for the payment of the Bonds the Authority's rights, title and interest in the Installment Payments (with certain exceptions), including the right to receive Installment Payments to be made by the City under the Installment Sale Agreement.

THE BONDS ARE LIMITED OBLIGATIONS OF THE AUTHORITY PAYABLE SOLELY FROM, AND SECURED BY, A PLEDGE OF, REVENUES AND CERTAIN FUNDS AND ACCOUNTS HELD UNDER THE TRUST AGREEMENT. THE AUTHORITY HAS NO TAXING POWER. THE CITY'S OBLIGATION TO PAY INSTALLMENT PAYMENTS IS A SPECIAL OBLIGATION OF THE CITY LIMITED SOLELY TO THE NET REVENUES. NO OTHER FUNDS OR PROPERTY OF THE CITY ARE LIABLE FOR THE PAYMENT OF THE INSTALLMENT PAYMENTS OR ANY OTHER AMOUNTS PAYABLE UNDER THE INSTALLMENT SALE AGREEMENT OR THE TRUST AGREEMENT. NEITHER THE BONDS NOR THE OBLIGATION OF THE CITY TO MAKE INSTALLMENT PAYMENTS CONSTITUTES AN INDEBTEDNESS OF THE AUTHORITY, THE CITY, THE STATE OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL DEBT LIMITATION.

Pledge of Net Revenues; Water Revenue Fund

Pursuant to the Installment Sale Agreement, all Net Revenues (see definition below) are irrevocably pledged to the payment of the Installment Payments and for the benefit of the Bond Owners and Owners of any outstanding obligations payable from Net Revenues on a parity with the Installment Payments ("Parity Obligations"). The City's obligation to pay the Installment Payments out of revenues of the Water System is ranked on a parity with the 2003 Loan and is subordinate to the City's obligations with respect to the 1999 Installment Payments. As of September 30, 2004, the remaining outstanding principal amount of the 2003 Loan is \$1,470,437 and the remaining aggregate unpaid principal amount of the 1999 Installment Payments is \$4,360,000.

Under the Installment Sale Agreement, the City covenants that all Gross Revenues will be deposited, upon receipt, in a fund designated as the "Water Revenue Fund," which fund is held separately from other funds of the City so long as any Installment Payments remain unpaid. All Gross Revenues

deposited in the Water Revenue Fund shall be applied, first, to pay Operation and Maintenance Costs as they become due and payable (including amounts reasonably required to be set aside in contingency reserves for Operation and Maintenance Costs, the payment of which is not then immediately required). No later than five Business Days before each Interest Payment Date, the City will transfer Net Revenues, in such amount as required under the Installment Sale Agreement, from the Water Revenue Fund to the Trustee for deposit in the Bond Fund to pay debt service then due on the Outstanding Bonds and Additional Bonds (defined below, see “Additional Bonds”) and replenishment of the Reserve Account.

Certain Definitions. The terms “Net Revenues,” “Gross Revenues” and “Operation and Maintenance Costs” are defined in the Installment Sale Agreement as follows:

“Net Revenues” means, for any period, an amount equal to all of the Gross Revenues received during such period minus the amounts required to pay all Operation and Maintenance Costs and the 1999 Installment Payments becoming payable during such period.

“Gross Revenues” means all income, rents, rates, fees, charges and other moneys derived from the ownership or operation of the Water System, including, without limiting the generality of the foregoing, (i) all income, rents, rates, fees, charges, business interruption insurance proceeds or other moneys derived by the City from the sale, furnishing and supplying of the water or other services, facilities, and commodities sold, furnished or supplied through the facilities of or in the conduct or operation of the business of the Water System, (ii) the earnings on and income derived from the investment of such income, rents, rates, fees, charges, or other moneys, including City reserves, (iii) the proceeds of any stand-by or water availability charges collected by the City, and (iv) the proceeds of any facilities fees or connection fees collected by the City, but excluding in all cases (A) customers’ deposits or any other deposits or advances subject to refund until such deposits or advances have become the property of the City, (B) any proceeds of taxes restricted by law to be used by the City to pay bonds hereafter issued, and (C) revenues from any surcharge that have been designated by the City for use for specific purposes, including with limitation, the perchlorate-related surcharge imposed pursuant to Resolution No. 5766, adopted by the City Council on February 4, 2004.

“Operation and Maintenance Costs” means the reasonable and necessary costs paid or incurred by the City for maintaining and operating the Water System, determined in accordance with generally accepted accounting principles, including all reasonable expenses of management and repair and all other expenses necessary to maintain and preserve the Water System in good repair and working order, and including all administrative costs of the City that are charged directly or apportioned to the operation of the Water System, such as salaries and wages of employees, overhead, taxes (if any), the cost of permits and licenses to operate the Water System and insurance premiums, and including all other reasonable and necessary costs of the City or charges required to be paid by it to comply with the terms hereof; but excluding in all cases (i) depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles, and (ii) any costs covered by revenues from surcharges described in clause (C) of the definition of “Gross Revenues.”

Rate Covenant

The City covenants under the Installment Sale Agreement that, while the Bonds remain Outstanding, the City will fix, prescribe, revise and collect rates, fees and charges for the services and facilities furnished by the Water System during each Fiscal Year, to yield Gross Revenues which will be at least sufficient, after making allowances for contingencies and error in the estimates, to pay the following amounts in the following order of priority:

- (A) All Operation and Maintenance Costs estimated by the City to become due and payable in such Fiscal Year;
- (B) The 1999 Installment Payments as they become due and payable during such Fiscal Year;
- (C) The Installment Payments and the principal of, and interest on, then outstanding Parity Obligations as they become due and payable during such Fiscal Year, without preference or priority (except to the extent such Installment Payments or such principal and interest on Parity Obligations are payable from the proceeds of the Bonds or Parity Obligations, or from any other source of legally available funds of the City which have been deposited with the Trustee for such purpose prior to the commencement of such Fiscal Year);
- (D) All amounts, if any, required to restore the balance in the Reserve Account to the full amount of the Reserve Requirement; and
- (E) All Additional Payments (consisting of certain payments to be made by the City to the Authority and the Trustee pursuant to the Installment Sale Agreement) and other payments required to meet any other obligations of the City which are charges, liens, encumbrances upon, or which are otherwise payable, from Gross Revenues during such Fiscal Year.

The City also covenants that, while the Bonds remain Outstanding, the City will fix, prescribe, revise and collect rates, fees and charges for the services and facilities furnished by the Water System during each Fiscal Year, so that Gross Revenues, less Operation and Maintenance Costs, will be at least equal to 120 percent of the sum of the amounts described in items (B) and (C) of the preceding paragraph. See “APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Installment Sale Agreement – Other Covenants of the City – Rates and Charges.”

Application of Revenues under Trust Agreement

Pursuant to the Trust Agreement, Revenues received by the Trustee in connection with an optional prepayment under the Installment Payment Agreement will be deposited in the Redemption Fund and used to pay the redemption price of any Bonds called pursuant to an optional redemption. See “THE BONDS – Redemption – *Optional Redemption*.” All other Revenues received by the Trustee will be deposited in the Bond Fund. On or before each Interest Payment Date, the Trustee will transfer from the Bond Fund and set aside in the following respective accounts in the amounts specified in the Trust Agreement in the following order of priority:

- (a) Interest Account (to pay interest coming due on the Bonds and all other outstanding Parity Bonds),
- (b) Principal Account (to pay principal, if any, of the Bonds and all other outstanding Parity Bonds maturing on such Interest Payment Date),
- (c) Sinking Account (to pay principal then coming due on the Term Bonds that are required to be redeemed on such Interest Payment Date), and
- (d) Reserve Account (to bring the balance thereof to an amount equal to the Reserve Requirement).

On or before June 15 and December 15 of each year the Trustee will determine the amount, if any, remaining in the Bond Fund after making the deposits required by the Trust Agreement. The Trustee

will apply such remaining amount as a credit against the next following Installment Payments; provided that, if directed in writing by the City, the Trustee will, with respect to all or any portion of such amount, (i) pay, or set an amount aside for the payment of, rebate in accordance with a computation made by the City pursuant to the Installment Sale Agreement; (ii) transfer an amount to the Project Fund, or (iii) transfer to the City to be used for any lawful purpose.

See “APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Trust Agreement – Establishment and Administration of Certain Funds and Accounts.”

Reserve Account

Pursuant to the Trust Agreement, a Reserve Account will be established and maintained by the Trustee in an amount equal to the Reserve Requirement. The Reserve Requirement as defined in the Trust Agreement means, as of any date of calculation, the least of (a) ten percent of the proceeds (within the meaning of Section 148 of the Code) of that portion of Outstanding Bonds and additional parity bonds issued pursuant to the Trust Agreement with respect to which Annual Debt Service is calculated, (b) 125 percent of Average Annual Debt Service, or (c) Maximum Annual Debt Service. Notwithstanding the foregoing, subject to the Trust Agreement, the Reserve Requirement, or a portion thereof, may be satisfied by one or more insurance policies, surety bonds, irrevocable and unconditional letters of credit, standby purchase agreements, lines of credit or other similar credit arrangements, if the Authority or the City furnishes the Trustee with written evidence that the use of such policies, instruments or arrangements will not by itself result in a downgrading or withdrawal of any credit rating then in effect with respect to the Bonds.

Upon issuance of the Bonds, the Trustee will deposit \$ _____ * from the sale proceeds of the Bonds into the Reserve Account, which amount is equal to the initial Reserve Requirement. Thereafter, on or before each Interest Payment Date, after the required deposits to the Interest Account, Principal Account and Sinking Account have been made, the Trustee will deposit Revenues in the Reserve Account in such amount as may be necessary to maintain a balance therein equal to the Reserve Requirement. Except as otherwise provided in the Trust Agreement, all money in the Reserve Account will be used and withdrawn by the Trustee for the purpose of (i) paying interest, principal or sinking account redemption payment on the Bonds in the event that the amounts in the Interest Account, the Principal Account and/or the Sinking Account are insufficient for such purposes or (ii) retiring all Bonds then Outstanding. Any amount in the Reserve Account in excess of the Reserve Requirement will be transferred to the Bond Fund.

See “APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Trust Agreement – Establishment and Administration of Certain Funds and Accounts – *Application of Reserve Account*.”

Additional Bonds

The Authority may from time to time issue additional bonds (“Additional Bonds”) payable on a parity with the Bonds, subject to the conditions precedent set forth in the Trust Agreement. Such conditions include, among other things, receipt by the Trustee of an opinion of Bond Counsel to the effect that the execution and delivery of the related supplement to the Trust Agreement and the related amendment to the Installment Sale Agreement will not adversely affect the tax-exempt status of the then Outstanding Bonds. See “APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Trust Agreement – Issuance of Additional Bonds.” The issuance of Additional Bonds in conjunction with the incurrence of additional obligations payable from Net Revenues on a parity with the Installment

* Preliminary; subject to change.

Payments (“Additional Parity Obligations”) is subject to the conditions precedent set forth in the Installment Sale Agreement, as described below.

Additional Obligations Payable from Net Revenues

Pursuant to the Installment Sale Agreement, so long as the Bonds are Outstanding, the incurrence of Additional Parity Obligations is subject to the following conditions precedent:

- (i) The City shall be in compliance with all covenants in the Installment Sale Agreement;
- (ii) No Event of Default under the Installment Sale Agreement and no event of default under the 1999 Installment Sale Agreement or with respect to any Parity Obligations shall have occurred and be continuing;
- (iii) The Net Water Revenues, together with any available property tax revenues, received by the City in the most recent Fiscal Year for which audited financial statements are available, shall be at least equal to 120 percent of the sum of the Maximum Annual Debt Service with respect to the 1999 Installment Payments (as defined in the 1999 Installment Sale Agreement) plus the Maximum Annual Debt Service with respect to the Installment Payments and any Parity Obligations which will be outstanding immediately following the incurrence of such Parity Obligations, as evidenced by a Report of an Independent Accountant or Fiscal Consultant; and
- (iv) If required by the terms of such Parity Obligation, a separate reserve has been or will be established therefor and that provisions have been made to fund such reserve.

The foregoing conditions do not apply to, or in any way limit, the City’s ability to incur Parity Obligations at any time to refund any outstanding Installment Payments or Parity Obligations, if such refunding will result in a net present value savings to the City (inclusive of all costs of such refunding).

The City covenants under the Installment Sale Agreement that, so long as any Bonds remain Outstanding, the City will not issue or incur any additional bonds or other obligations which will rank senior in the priority of lien over the Installment Payments with respect to the Net Revenues. The Installment Sale Agreement does not in any way limit the City’s ability to incur obligations which rank junior to the Installment Payments in their lien with respect to the Net Revenues.

See “APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS – Installment Sale Agreement – Additional Parity Obligations.”

BOND INSURANCE

The following information has been furnished by _____ for use in this Official Statement. Such information has not been independently confirmed or verified by the Authority or the City. The Authority and the City make no representation as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof. Reference is made to Appendix G for a specimen of the Bond Insurance Policy.

[to come]

THE WATER SYSTEM

Organization and Management

The City provides water services to its residents through its Public Works Department. The responsibility and powers of the Public Works Department with respect to the Water System, including the establishment of rates and charges, are exercised through the City Council. The Director of Public Works oversees the day-to-day operation of the Public Works Department and reports to the City Manager. The City's Director of Finance works closely with the City Manager and the director of each City Department, such as the Director of Public Works, to prepare periodic revenue and expenditure reports, revenue projections and make budget recommendations for all City department and enterprises, including the Water System. Below are brief biographies of the City Manager, the Director of Finance and the Director of Public Works:

J. Edward Tewes, City Manager. Mr. Tewes was appointed City Manager of the City in January 2000, bringing over 30 years of municipal management experience in four California communities. He earned a Bachelor's of Arts degree in political science from Claremont Men's College in 1972, and a Masters of Public Administration degree from the University of Southern California in 1974. Mr. Tewes is a member of the International City/County Management Association. He is currently a member, and in the past served as the President, of the Board of Directors of the California Redevelopment Association.

Jack Dilles, Director of Finance. Mr. Dilles was appointed Director of Finance of the City in April 2000, bringing over 20 years of governmental financial and management experience. He earned a Bachelor's of Science degree in business administration in 1977 and a Masters of Business Administration degree in 1988, both from San Jose State University. Mr. Dilles is a member of the Governmental Finance Officers Association ("GFOA"), California State Municipal Finance Officers, and California Municipal Treasurers Association. He is a Certified Public Finance Officer, conferred by the GFOA.

Jim Ashcraft, Director of Public Works. Mr. Ashcraft was appointed Director of Public Works of the City in August 2000, bringing over 20 years of experience directing the construction and operations of three California cities' municipal water system. He earned a Bachelor's of Science degree in civil engineering in 1976 from California Polytechnic University. Mr. Ashcraft is a member of the American Public Works Association and American Water Works Association. He is a Registered Civil Engineer in the State of California.

Service Area

The City provides potable water service to its residential and commercial/industrial customers within the City limits and some adjacent unincorporated county areas. The Service Area is currently approximately six miles across from east to west and five and one-half miles across from north to south. Most of the City is on relatively flat valley land, with some developments in the foothill areas both east and west of the valley floor. Elevations of the Service Area range from approximately 350 feet on the valley floor to over 1,200 feet in the foothills. However, most of the Service Area is within the valley floor at an elevation of 310 to 400 feet. In order to maintain appropriate operating pressures at different locations, the Service Area is divided into multiple pressure zones, with gates and pressure reducing valves being used to isolate or regulate the flow between the pressure zones. There are currently 13 different pressure zones in the Service Area.

Water Supply

The Water System currently relies on groundwater to meet all of its supply needs. The City extracts water from underground aquifers via the groundwater wells that are distributed along the valley floor. There are 13 groundwater wells in the Water System, three of which are currently inactive. See “Environmental Issues – Perchlorate.” The Water System’s 13 groundwater wells have an estimated total capacity of 12.9 million gallons per day (“MGD”), and the 11 currently active wells have an estimated combined capacity of 11.5 MGD. All of the groundwater wells are located within two of the pressure zones. Booster stations are used to lift water up to the east and west foothills pressure zones. Pressure reducing valves and gate valves are used to convey and allow the water to flow to the other zones.

The City draws water from depths ranging between 120 and 400 feet below the surface, tapping the Llagas Subbasin which underlies the southern Santa Clara Valley. The Llagas Subbasin covers an area of approximately 74 square miles, extending from Cochrane Road of the City to the County’s southern boundary. The Llagas Subbasin has an estimated capacity of 475,000 acre feet, or 154,780 million gallons (“MG”) (one acre-feet equaling approximately 325,851 gallons). Water drawn from the Llagas Subbasin is replaced by rainfall and an active recharge program operated by the Santa Clara Valley Water District (the “SCVWD”). The recharge program is financed through a groundwater pump tax paid by the City and other SCVWD customers drawing from the subbasin. The Water System Consultant noted in the 2002 Master Plan that the Llagas Subbasin appears to be subject to both fairly rapid lowering of groundwater depths during dry years as well as rapid recovery during the wet years.

The following table sets forth the approximate volume of water produced from the Water System’s groundwater wells in each of fiscal years 1999-00 through 2003-04. As of September 1, 2004, the SCVWD pump tax payable by the City is \$200 per 100 cubic feet (“HCF”). The rate of the pump tax is adjusted by SCVWD from time to time and is not subject to the City’s control.

Table 1
CITY OF MORGAN HILL
Water Production
Fiscal Years 1999-00 through 2003-04

	<u>1999-00</u>	<u>2000-01</u>	<u>2001-02</u>	<u>2002-03</u>	<u>2003-04</u>
Total Production (in acre feet)					
Increase from Prior Year	-	%			

Source: City of Morgan Hill

See “Demand and Requirement Projections” and “Capital Improvement Program” below for discussions of the Water System Consultant’s evaluation of the City’s supply capacity in light of projected requirements of the Water System and certain proposed capital improvements to meet such requirements.

Storage and Distribution System

The Water System storage and distribution facilities include 10 water storage tanks, 10 booster stations, and over 160 miles of pressured pipes ranging from two to 14 inches in diameter. The City's 10 ground level storage tanks have a combined capacity of 5.23 MG. The storage system services the City's operational, fire reserve, and emergency needs. Operational storage regulates fluctuations in demand. Fire reserve storage regulates fire flow demands. Emergency storage meets demands during emergency situations such as pipeline failures, major trunk main failures, pump failures, electrical power outages, or natural disasters. Water is conveyed from the lower pressure zones to the higher pressure zones via a series of booster stations. Gates and pressure reducing valves are used to isolate or regulate flow between pressure zones.

See "Demand and Requirement Projections" and "Capital Improvement Program" below for discussions of the Water System Consultant's evaluation of the City's storage and distribution capacities with respect to projected requirements of the Water System and certain proposed capital improvements to meet such requirements.

Customers; Customer Usage

The following two tables summarize the customer usage by volume (in 100 cubic feet ("HCF")) and the number of customer accounts with respect to the Water System from fiscal years 1999-00 through fiscal years 2003-04:

Table 2
CITY OF MORGAN HILL WATER SYSTEM
Customer Usage by Volume (in HCF)
Fiscal Years 1999-00 through 2003-04

<u>Customer Type</u>	<u>1999-00</u>	<u>2000-01</u>		<u>2001-02</u>		<u>2002-03</u>		<u>2003-04</u>	
	<u>Vol.</u>	<u>Vol.</u>	<u>% Change</u>	<u>Vol.</u>	<u>% Change</u>	<u>Vol.</u>	<u>% Change</u>	<u>Vol.</u>	<u>% Change</u>
Residential									
Single family									
Multifamily									
<u>Commercial/Industrial</u>									
Total									

Source: City of Morgan Hill.

Table 3
CITY OF MORGAN HILL WATER SYSTEM
Number of Customer Accounts
Fiscal Years 1999-00 through 2003-04

	<u>1999-00</u>		<u>2000-01</u>		<u>2001-02</u>		<u>2002-03</u>		<u>2003-04</u>	
<u>Customer Type</u>	<u>No. of</u>		<u>No. of</u>	<u>%</u>	<u>No. of</u>	<u>%</u>	<u>No. of</u>	<u>%</u>	<u>No. of</u>	<u>%</u>
	<u>Accts</u>		<u>Accts</u>	<u>Change</u>	<u>Accts</u>	<u>Change</u>	<u>Accts</u>	<u>Change</u>	<u>Accts</u>	<u>Change</u>
Residential										
Single family										
Multifamily										
<u>Commercial/Industrial</u>										
Total										

Source: City of Morgan Hill.

Rates, Charges and Fees

The City recovers the cost of Water System operation, maintenance and replacement, and capital expansion through a user fee system. The components of the user fees currently imposed by the City include commodity charges (based on usage), service charges (flat monthly rates), connection fees and miscellaneous fees and charges. See “CONSTITUTIONAL LIMITATIONS AFFECTING WATER SYSTEM REVENUES AND EXPENDITURES – Proposition 218: Article XIIC and Article XIID – *Water Service Fees and Charges.*”

Commodity and Service Charges. The current rates for the City’s water commodity and service charges became effective on January 1, 2004 and were established by City Council Resolution No. 5638, adopted on February 3, 2003, as modified by Resolution No. 5766, adopted on February 4, 2004. Resolution No. 5766 provides that such rates will increase on January 1st of each of 2005, 2006 and 2007 by the amounts prescribed in such resolution, unless based on the Director of Finance’s report (to be made by September 30th of each year), the City Council makes a determination to eliminate the two percent increase for the following January 1st. The current rates were established, based on a report entitled “Water and Sewer Fund Revenue Requirement Study,” dated October 17, 2002 (the “2002 Rate Study”), prepared by Hilton Frankopf & Hobson, LLC, and further analyses done in 2003 by the City’s Finance Department, to meet projected revenue requirements for the Water System. The City’s rate structures for water commodity and service charges are designed, in part, to encourage water conservation. The following two tables show the City’s commodity and service charges rates, as set forth in Resolution No. 5766:

Table 4
CITY OF MORGAN HILL WATER SYSTEM
Commodity Charge Rates ⁽¹⁾
(Based on Monthly Usage)

<u>Property Type</u>	<u>2004</u>		<u>2005 ⁽²⁾</u>		<u>2006 ⁽²⁾</u>		<u>2007 ⁽²⁾</u>	
	<u>Inside City</u>	<u>Outside City</u>	<u>Inside City</u>	<u>Outside City</u>	<u>Inside City</u>	<u>Outside City</u>	<u>Inside City</u>	<u>Outside City</u>
<i>Residential (per dwelling unit per HCF) ⁽³⁾</i>								
<u>Single-family</u>								
1-10 HCF	\$0.99	\$1.53	\$1.01	\$1.56	\$1.03	\$1.59	\$1.05	\$1.62
11-30 HCF	1.98	3.07	2.02	3.13	2.06	3.19	2.10	3.26
30+ HCF	2.97	4.60	3.03	4.69	3.09	4.79	3.15	4.88
<u>Multifamily</u>								
1-8 HCF	0.99	1.53	1.01	1.56	1.03	1.59	1.05	1.62
9-16 HCF	1.98	3.07	2.02	3.13	2.06	3.19	2.10	3.26
17+ HCF	2.97	4.60	3.03	4.69	3.09	4.79	3.15	4.88
<i>Non-Residential (per HCF)</i>								
All uses	1.61	2.50	1.64	2.55	1.68	2.60	1.71	2.65

(1) As established by Resolution No. 5766, adopted on February 4, 2004.

(2) Assumes a two percent increase from the prior year, see narrative above. Becomes effective as of January 1st of such year.

(2) 100 cubic feet equals approximately 748 gallons.

Source: City of Morgan Hill

Table 5
CITY OF MORGAN HILL WATER SYSTEM
Service Charge Rates ⁽¹⁾
(Flat Monthly Rates)

<u>Meter size (inches)</u>	<u>2004</u>		<u>2005 ⁽²⁾</u>		<u>2006 ⁽²⁾</u>		<u>2007 ⁽²⁾</u>	
	<u>Inside City</u>	<u>Outside City</u>	<u>Inside City</u>	<u>Outside City</u>	<u>Inside City</u>	<u>Outside City</u>	<u>Inside City</u>	<u>Outside City</u>
5/8"	\$ 5.10	\$7.91	5.20	8.07	5.31	8.23	5.41	8.39
3/4	5.10	7.91	5.20	8.07	5.31	8.23	5.41	8.39
1	5.10	7.91	5.20	8.07	5.31	8.23	5.41	8.39
1 1/2	8.48	13.16	8.65	13.42	8.82	13.69	9.00	13.97
2	13.63	21.12	13.90	21.54	14.18	21.97	14.46	22.41
3	27.21	42.19	27.75	43.03	28.31	43.89	28.88	44.77
4	44.06	68.30	44.94	69.67	45.84	71.06	46.76	72.48
6	67.68	105.08	69.03	107.18	70.41	109.33	71.82	111.51
8	101.70	157.62	103.73	160.77	105.81	163.99	107.92	167.27
10	135.62	210.21	138.33	214.41	141.10	218.70	143.92	223.08
Low income discounts	(3.07)	(3.07)	(3.13)	(3.13)	(3.19)	(3.19)	(3.26)	(3.26)

(1) As established by No. 5766, adopted on February 4, 2004.

(2) Assumes a two percent increase from the prior year, see narrative in the text above Table 4. Becomes effective as of January 1st of such year.

Source: City of Morgan Hill

Connection Fees. The City's current rates for water connection fees were established by City Council Resolution No. 5592, adopted on August 21, 2002, after a review of the 2002 Rate Study. The fee increase imposed by Resolution No. 5592 was designed to be "phased-in" over a three year period, beginning January 15, 2003. The City considers the water connection fee to be a development impact fee. Similar to most other development impact fees charged by the City, the connection fee is adjusted automatically each year in accordance with Section 3.56.050 of the City's Municipal Code. Section 3.56.050 of the City's Municipal Code, as amended, provides that, on January 15th of each year, the rates for the City's development impact fees, except for the police impact fee, are adjusted by a percentage equal to the Engineering Cost Index as published by Engineer News Record for the 12-month period ending the previous March. The table below shows the rates for the City's water connection fees in effect for 2004 and 2005, which is the last year the "phase-in period" under Resolution No. 5592:

Table 6
CITY OF MORGAN HILL WATER SYSTEM
Connection Fees⁽¹⁾

<u>Type of Development</u>	<u>2004⁽²⁾</u>	<u>2005⁽³⁾</u>
Residential		
Single family – subdivision (per unit)	\$1,648	\$1,899
Single family – no subdivision (per unit)	1,648	1,899
Multifamily – subdivision (per unit)	1,487	1,714
Multifamily – no subdivision (per unit)	1,478	1,714
Commercial (per acre)	4.678	5.394
Industrial (per acre)	4.678	5.394

(1) As established by No. 5592, adopted on August 21, 2002.

(2) Effective as of January 15, 2004.

(3) To become effective January 15, 2005. Excludes the adjustment to be made pursuant to Section 3.56.050 of the City's Municipal Code. For reference only: The Section 3.56.050 adjustments for the rates which became effective January 15, 2004 were __ percent for single family residential properties, __ percent for multifamily residential properties, __ percent for commercial properties and __ percent for industrial properties.

Source: City of Morgan Hill

Perchlorate Cost Surcharge. In addition to the fees and charges described above, the City Council, by Resolution No. 5766, also approved a surcharge to be added to all commodity and service charges in light of the unexpected costs relating to the discovery of perchlorate contamination. As discussed in more detail under "Environmental Issues – *Perchlorate*," the contaminant perchlorate was discovered in one of the City's groundwater wells in May 2002. Since that time, the City has taken, and continues to take, actions relating to testing, clean-up and other measures to protect the quality of the City's water supply. Revenues from the surcharge are segregated and intended to be spent only on perchlorate related costs.

Pursuant to Resolution No. 5766, the five percent perchlorate cost surcharge became effective April 1, 2004, and will be increased by an additional five percent on January 1st of each of 2005, 2006 and 2007, unless otherwise directed by the City Council. The perchlorate cost surcharge may be eliminated, if the City Council determines, after a review of the Director of Finance's report, that the amount of perchlorate cost surcharge revenues on hand exceeds the amount then needed to finance all of the City's anticipated perchlorate related costs. Resolution No. 5766 also provides that any amount determined by the City Council to be in excess of the amount needed to finance all anticipated perchlorate related costs, based on the Director of Finance's report, will be refunded to customers through future across-the board percentage rate reductions to be approved by the City Council.

Comparative Rates. The following table compares the commodity charge, service charge and connection fee for a typical single family residential unit imposed by the City and those of certain other communities [and agencies] in the [County] as of _____, 2004:

Table ____
CITY OF MORGAN HILL WATER SYSTEM
Comparative Rates
(Based on a Typical Single Family Residential Unit)
as of _____, 2004

<u>Community</u>	<u>Monthly Usage Charge ⁽¹⁾</u>	<u>Monthly Service Charge ⁽²⁾</u>	<u>Connection Fee</u>
Morgan Hill			

(1) Assumes use of _____ cubic feet per month. Excludes perchlorate cost surcharge.

(2) Assumes meter size of _____. Excludes perchlorate cost surcharge.

Source: Black & Veatch, _____ report.

Billing and Collection

Customers are billed on a monthly basis for approximately 30 day periods. Bills are due upon presentation and are considered delinquent after 25 days. If the amount due is unpaid after 25 days, a late charge of 1.5 percent of the current charges are assessed. If payment is not made within 35 days of the original billing, a late notice is mailed to the customer stating the date on which service will be terminated if the account is not brought current and a \$12 fee is charged. The customer is allowed 10 days after the notice is mailed to pay, or service will be terminated. The customer is required to pay outstanding fees and charges, including a \$39 reconnect fee, before water service is restored. For fiscal year 2002-03, the amount of the City's write-off as the result of Water System customer delinquencies was \$27,553.

Demand and Requirement Projections

In the 2002 Master Plan, the Water System Consultant provided (a) an evaluation of the Water System's supply, storage and distribution capacities, (b) projections regarding the demands on the Water System through the year 2020 and (c) recommendations on a capital improvement program that would allow the City to meet its projected demands. The Water System Consultant followed the assumptions made by the City's existing General Plan with respect to population growth, *i.e.*, that the City's population will reach 38,800 and 48,000 in 2010 and 2020, respectively, which are the ceilings established by the City's residential growth control program. See "APPENDIX A – SUPPLEMENTAL INFORMATION ABOUT THE CITY OF MORGAN HILL – Population – *Residential Development Control System.*" The Water System Consultant concluded in the 2002 Master Plan that additional supply and storage capacities were needed to adequately meet the existing and future water demands on the Water System. While the Water System Consultant believed that the City's water distribution system was sufficient for existing customer needs, enhancements were also recommended. See "Capital Improvement Program" below.

The table below summarizes the projected demand and supply requirements on the Water System between 2005 and 2020, as set forth in the 2002 Master Plan:

Table 7
CITY OF MORGAN HILL WATER SYSTEM
Projected Demand and Supply Requirements
Calendar Years 2005 through 2020

	<u>Actual</u>	<u>Projected</u>			
	<u>2000</u>	<u>2005</u>	<u>2010</u>	<u>2015</u>	<u>2020</u>
Projected population	33,092	36,500	38,800	43,400	48,000
Projected demand (in MGD)					
Average day demand	6.6	7.3	7.8	8.7	9.6
Maximum day demand	13.2	14.6	15.5	17.4	19.2
Peak hour demand	21.2	23.4	24.8	27.8	30.7
Supply requirements (in MGD)					
Required supply ⁽¹⁾	15.0	16.4	17.3	19.2	21.0
Total available supply in 2001	13.1	-	-	-	-
Firm available supply in 2001 ⁽²⁾	11.1	-	-	-	-

(1) Based on maximum day demand, plus 1.8 MGD standby.

(2) Equals total available supply in 2001, less 1,500 gallons per minute standby.

Source: City of Morgan Hill Water System Master Plan, January 2002.

Capital Improvement Program

The City intends to proceed with the capital improvements recommended by the Water System Consultant in the 2002 Master Plan. The recommended improvements include five new groundwater wells, eleven storage tanks, ten booster stations and certain amounts of pipes, casing and pressure reducing valves. The proposed new groundwater wells, with an individual average capacity of 1.5 MGD, are expected to provide the City with 21.0 MGD of firm supply capacity by 2020. The proposed new storage tanks, ranging from 0.2 MG to 1.50 MG in volume, are expected to provide the City with an additional 3.25 MG of storage capacity by 2020. As of July 2004, the City has completed the installation of one 4.0 MG storage tank. Proceeds from the sale of the Bonds are expected to be used to finance the costs of a portion of the remaining recommended capital improvements. See "PLAN OF FINANCING."

Environmental Issues

The applicable drinking water standards for the Water System are contained in the California Domestic Water Quality and Monitoring Regulations, Title 22 of the California Administrative Code. These regulations incorporate the requirements of the United States Environmental Protection Agency ("USEPA") in conformance with the federal Safe Drinking Water Act. The standards specify water quality sampling frequencies and locations as well as maximum concentrations of chemical constituents. They are continuously being revised and amended. The drinking water quality of the City meets all State of California Department of Health Services and USEPA drinking water standards set to protect public health.

Perchlorate. Perchlorate is an inorganic contaminant of drinking water. According to materials published by the California Office of Environmental Health Hazard Assessment, perchlorate can limit the uptake of iodide, an essential nutrient, by the thyroid gland, thereby disrupting thyroid hormones that regulate metabolism and growth.

The Director of Public Works announced at the May 22, 2002 City Council meeting that the City discovered perchlorate in one of the City's groundwater wells, known as the Tennant Well. The City

responded to the discovery by closing the Tennant Well, testing all City wells for the presence of perchlorate on a monthly basis, temporarily closing the Nordstrom and Condit Wells, and installing a perchlorate removal plant at the Nordstrom Well. Since June 25, 2003, the City Manager has reported that no water samples taken from active City wells have tested above the state detection level.

While the water supplied by the City remains in full compliance with all State and Federal safety standards, the City is taking additional measures to protect the water supply. As of June 30, 2004, the City has spent approximately \$1.5 million on drilling wells, building perchlorate plants, and monitoring perchlorate in the water supply. The City expects to spend a total of \$3.9 million on perchlorate-related costs by June 2007. In order to meet the additional costs created by these measures, the City Council approved a surcharge, the revenues from which revenues will be accounted for separately and spent only on perchlorate related costs. See “Fees, Rates and Charges – *Perchlorate Surcharge*.”

The City has identified a site (the “Olin Site”) formerly owned by the Olin Corporation (“Olin”) as the source of the perchlorate contamination. The Olin Site is a 13-acre parcel located in southern part of the City. Olin, and subsequently its lessee, manufactured signal flares at the facility for from 1956 to 1995. Potassium perchlorate was used in the manufacture of flares. The City has been negotiating with Olin regarding reimbursement for the City’s costs relating to the perchlorate contamination. As of September 27, 2004, Olin has reimbursed the City \$715,146, and has agreed to pay the City for an additional \$65,682, for perchlorate-related costs. The City is attempting to collect from Olin additional reimbursements, up to the entire perchlorate-related cost incurred or to be incurred by the City, through further negotiation and legal actions, as necessary. Despite the City’s efforts, there is no guarantee that the City will be ultimately successful in collecting a full reimbursement from Olin.

Insurance

Insurance with respect to the Water System is covered under the City’s general policies. The City is a member of the Association of Bay Area Governments (“ABAG”). The City participates in ABAG’s Pooled Liability Insurance Network (the “ABAG-PLAN”), a self-insured risk pool formed by certain cities in California to pool their insurance risk and help lower the overall cost of providing insurance coverage for general liability claims. The coverage amount is \$10 million per occurrence, subject to a \$100,000 deductible. The City Manager, the Director of Finance as Risk Manager, and the City Attorney work with the ABAG-PLAN to coordinate the City’s insurance policies, maintain insurance records and represent the City in handling claims. In addition, the City is fully self-insured for unemployment insurance. The City is also self-insured for workers’ compensation up to a maximum of \$250,000 for each claim. Purchased insurance covers the excess of \$5,000,000 per year for workers’ compensation claims.

WATER SYSTEM FINANCIAL INFORMATION

Financial Statements

Set forth in Tables 8 and 9 below are the Statements of Net Assets and the Statements of Revenues, Expenditures and Changes in Fund Balances with respect to the Water Revenue Fund from fiscal years 1999-00 through 2002-03, based on the City's audited financial statements. Such statements are subject to various notes attached to the City's financial statements for the respective years. Excerpts of the City's Comprehensive Annual Financial Report for fiscal year ended June 30, 2003, which includes the City's 2002-03 audited financial statements and the Independent Auditor's Report issued by Caporicci & Larson, Certified Public Accountants (the "Auditor") regarding such financial statements, is set forth in Appendix B. The City has not requested the Auditor to consent to the inclusion of its report in Appendix B and it has not undertaken to update financial statements included in Appendix B. A complete copy of the City's Comprehensive Annual Financial Report for fiscal year ended June 30, 2003, as well as the reports for the prior years, can be obtained from the City's Finance Department.

The accounting policies of the City conform to generally accepted accounting principles. The Governmental Accounting Standards Board ("GASB") published its Statement No. 34, "Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments" on June 30, 1999. Statement No. 34 provides guidelines to auditors, state and local governments and special purpose governments such as school districts and public utilities, on new requirements for financial reporting for all governmental agencies in the United States. Generally, the basic financial statements and required supplementary information should include the following:

- management's discussion and analysis (introducing the basic financial statements and providing an analytical overview of the government's financial activities);
- basic financial statements including (i) government-wide financial statements prepared using the economic resources measurement focus and the accrual basis of accounting; (ii) fund financial statements, which may include (A) governmental fund financial statements (including financial data for the general fund and special revenue, capital projects, debt service, and permanent funds), prepared using the current financial resources measurement focus and the modified accrual method of accounting, (B) proprietary fund financial statements (including financial data for enterprise and internal service funds) prepared using the economic resources measurement focus and the accrual basis of accounting, and (C) fiduciary fund financial statements (including financial data for fiduciary funds and similar component units) prepared using the economic resources measurement focus and the accrual basis of accounting; and (iii) notes to the financial statements; and
- required supplementary information.

The City implemented GASB Statement No. 34, beginning with audited financial statements for fiscal year 2002-03. Consequently, changes in financial statement content and structure are evident since the 2002-03 audit. In reviewing the tables below, readers should be mindful that the numbers presented for fiscal years 2000-01 through 2001-02 may not be directly comparable to those for fiscal years 2002-03 and 2003-04.

The City maintains two separate accounts within the Water Revenue Fund referred to in the audited financial statements as the "Water Operations Fund" (the "Operations Fund") and the "Water Mitigation Fund" (the "Mitigation Fund"). The Mitigation Fund was established for the convenience of

tracking revenues and expenditures relating to water development impact fees (*i.e.*, connection fees). See “THE WATER SYSTEM – Rates, Charges and Fees – Connection Fees”). Generally, development impact fees are used for costs relating to infrastructure improvements that is attributable to new growth. Following the format of the City’s audited financial statements, Tables 8 and 9 below use separate columns for the Operations Fund and the Mitigation Fund. The figures in the columns showing the total of the numbers under the column headings “Operations Fund” and “Mitigation Fund” are for the readers’ convenience only and do not appear in the City’s audited financial statements.

Table 8
CITY OF MORGAN HILL WATER SYSTEM
Statements of Net Assets
Fiscal Years 2000-01 through 2003-04 ⁽¹⁾

	2000-01			2001-02			2002-03			(unaudited) 2003-04		
	Operations Fund	Mitigation Fund	Total	Operations Fund	Mitigation Fund	Total	Operations Fund	Mitigation Fund	Total	Operations Fund	Mitigation Fund	Total
Assets:												
<i>Current assets</i>												
Pooled cash and invest.	\$7,749,902	\$ --	\$7,749,902	\$8,262,795	\$ --	\$8,262,795	\$6,665,161	\$ --	\$6,665,161	6,294,871	\$ --	\$6,294,871
Restricted pooled cash and investment	--	1,463,772	1,463,772	--	887,512	887,512	--	\$124,965	124,965	--	--	
Cash with fiscal agents	392,791	--	392,791	390,888	--	390,888	390,413	--	390,413	390,261	--	390,261
Receivables												
Accrued interest	128,365	24,280	152,645	45,832	4,426	50,258	40,430	724	41,154	24,424	--	24,424
Other accts receiv	<u>1,097,765</u>	<u>--</u>	<u>1,097,765</u>	<u>984,686</u>	<u>--</u>	<u>984,686</u>	<u>1,026,785</u>	<u>--</u>	<u>1,026,785</u>	<u>961,215</u>	<u>--</u>	<u>961,215</u>
<i>Total current assets</i>	<u>9,368,823</u>	<u>1,488,052</u>	<u>10,856,875</u>	<u>9,684,201</u>	<u>891,938</u>	<u>10,576,139</u>	<u>8,122,789</u>	<u>125,689</u>	<u>8,248,478</u>	<u>7,670,771</u>	<u>--</u>	<u>7,670,771</u>
<i>Non-current assets</i>	<u>28,147,884</u>	<u>1,278,357</u>	<u>29,426,241</u>	<u>27,892,044</u>	<u>1,970,306</u>	<u>29,862,350</u>	<u>28,858,792</u>	<u>3,386,162</u>	<u>32,244,954</u>	<u>28,858,792</u>	<u>4,518,188</u>	<u>33,376,980</u>
Total assets	<u>37,516,707</u>	<u>2,766,409</u>	<u>40,283,116</u>	<u>37,576,245</u>	<u>2,862,244</u>	<u>40,438,489</u>	<u>36,981,581</u>	<u>3,511,851</u>	<u>40,493,432</u>	<u>36,529,563</u>	<u>4,518,188</u>	<u>\$41,047,751</u>
Liabilities:												
<i>Current liabilities</i>												
Accounts payable	301,097	--	301,097	362,768	104,896	467,664	329,787	240,572	570,359	502,953	102,098	605,051
Accrued liabilities	50,097	--	50,097	51,869	--	51,869	62,097	--	62,097	76,012	--	76,012
Customer & other deposits	46,939	--	46,939	44,119	--	44,119	38,186	--	38,186	38,042	--	38,042
Current obligations - Bonds payable	210,320	--	210,320	219,332	--	219,332	166,607	--	166,607	261,807	--	261,807
Compensated absences	<u>9,189</u>	<u>--</u>	<u>9,189</u>	<u>16,797</u>	<u>--</u>	<u>16,797</u>	<u>6,482</u>	<u>--</u>	<u>6,482</u>	<u>9,776</u>	<u>--</u>	<u>9,776</u>
<i>Total current liab.</i>	<u>617,642</u>	<u>--</u>	<u>617,642</u>	<u>694,885</u>	<u>104,896</u>	<u>799,781</u>	<u>603,159</u>	<u>240,572</u>	<u>843,731</u>	<u>888,590</u>	<u>102,098</u>	<u>990,688</u>
<i>Noncurrent liabilities</i>												
Long term obligations - Bonds payable	5,129,781	--	5,129,781	4,969,270	--	4,969,270	4,861,483	--	4,861,483	4,590,476	--	4,590,476
Compensated absences	<u>58,034</u>	<u>--</u>	<u>58,034</u>	<u>48,088</u>	<u>--</u>	<u>48,088</u>	<u>82,477</u>	<u>--</u>	<u>82,477</u>	<u>81,777</u>	<u>--</u>	<u>81,777</u>
<i>Total noncurrent liab.</i>	<u>5,187,815</u>	<u>--</u>	<u>5,187,815</u>	<u>5,017,358</u>	<u>--</u>	<u>5,017,358</u>	<u>4,943,960</u>	<u>--</u>	<u>4,943,960</u>	<u>4,672,253</u>	<u>--</u>	<u>4,672,253</u>
Total liabilities	<u>5,805,457</u>	<u>--</u>	<u>5,805,457</u>	<u>5,712,243</u>	<u>104,896</u>	<u>5,817,139</u>	<u>5,547,119</u>	<u>240,572</u>	<u>5,787,691</u>	<u>5,560,843</u>	<u>102,098</u>	<u>5,662,941</u>
<i>Net Assets</i>												
Invested in cap. assets	22,960,069	1,278,357	24,238,426	22,874,686	1,970,306	24,844,992	23,914,832	3,271,279	27,186,111	24,186,539	4,416,090	28,602,629
Restricted cap. expan.	392,791	1,488,052	1,880,843	--	787,042	787,042	--	--	--	--	--	--
Unrestricted	<u>8,358,390</u>	<u>--</u>	<u>8,358,390</u>	<u>8,989,316</u>	<u>--</u>	<u>8,989,316</u>	<u>7,519,630</u>	<u>--</u>	<u>7,519,630</u>	<u>6,782,181</u>	<u>--</u>	<u>6,782,181</u>
Total Net Assets	<u>\$31,711,250</u>	<u>\$2,766,409</u>	<u>\$34,477,659</u>	<u>\$31,864,002</u>	<u>\$2,757,348</u>	<u>\$34,621,350</u>	<u>\$31,434,462</u>	<u>\$3,271,279</u>	<u>\$34,705,741</u>	<u>\$30,968,720</u>	<u>\$4,416,090</u>	<u>\$35,384,810</u>

(1) The City implemented GASB Statement No. 34 beginning with its financial statements for fiscal year 2002-03, therefore numbers presented for fiscal years 2000-01 through 2001-02 may not be directly comparable to those for fiscal years 2002-03 and 2003-04.

Source: City of Morgan Hill audited financial statements for fiscal years 2000-01 through 2003-04.

Table 9
CITY OF MORGAN HILL WATER SYSTEM
Statements of Revenues, Expenditures and Changes in Fund Balances
Fiscal Years 2000-01 through 2003-04

	2000-01			2001-02			2002-03			(unaudited) 2003-04		
	Operations Fund	Mitigation Fund	Total	Operations Fund	Mitigation Fund	Total	Operations Fund	Mitigation Fund	Total	Operations Fund	Mitigation Fund	Total
Operating Revenues:												
Charges - current services	\$5,955,510	\$55,632	\$6,011,142	\$5,915,530	\$204,296	\$6,119,826	\$6,184,207	\$162,865	\$6,347,072			
Total oper revenues	<u>5,955,510</u>	<u>55,632</u>	<u>6,011,142</u>	<u>5,915,530</u>	<u>204,296</u>	<u>6,119,826</u>	<u>6,184,207</u>	<u>162,865</u>	<u>6,347,072</u>			
Operating expenses:												
Salaries & benefits	1,166,000	--	1,166,000	1,276,946	--	1,276,946	1,356,985	--	1,356,985			
Utilities & taxes	1,349,127	--	1,349,127	1,790,527	--	1,790,527	--	--	--			
Claims & insur premium	--	--	--	--	--	--	912,023	--	912,023			
Oper and mainten	936,438	67,920	1,004,358	729,887	--	729,887	1,978,163	--	1,978,163			
Depreciation	1,109,507	55,575	1,165,082	1,424,193	252,224	1,676,417	1,147,373	123,325	1,270,698			
<u>Administrative charges</u>	<u>281,152</u>	<u>--</u>	<u>281,152</u>	<u>347,297</u>	<u>216</u>	<u>347,513</u>	<u>433,336</u>	<u>815</u>	<u>434,151</u>			
Total operating expenses	<u>4,842,224</u>	<u>123,495</u>	<u>4,965,719</u>	<u>5,568,850</u>	<u>252,440</u>	<u>5,821,290</u>	<u>5,827,880</u>	<u>124,140</u>	<u>5,952,020</u>			
Nonoper rev (expenses):												
Investment earnings	594,913	108,104	703,017	351,226	39,083	390,309	303,197	15,206	318,403			
Interest (expense)	(409,744)	--	(409,744)	(395,695)	--	(395,695)	(385,442)	--	(385,442)			
Total nonoper. rev./exp.	<u>185,169</u>	<u>108,104</u>	<u>293,273</u>	<u>(44,469)</u>	<u>39,083</u>	<u>(5,386)</u>	<u>(82,245)</u>	<u>15,206</u>	<u>(67,039)</u>			
Income (loss) before operating transfers	1,298,455	40,241	1,338,696	302,211	(9,061)	293,150	274,082	53,931	328,013			
Capital contributions	--	--	--	--	--	--	695,723	--	695,723			
Operating transfers in	2,009,213	--	2,009,213	2,590,541	--	2,590,541	1,373,878	460,000	1,833,878			
Operating transfers (out)	<u>(1,814,387)</u>	<u>(470,698)</u>	<u>(2,285,085)</u>	<u>(2,740,000)</u>	<u>--</u>	<u>(2,740,000)</u>	<u>(2,077,500)</u>	<u>--</u>	<u>(2,077,500)</u>			
Change in net assets	1,493,281	(430,457)	1,062,824	152,752	(9,061)	143,691	266,182	--	266,182			
Total net assets – begin.	<u>30,217,969</u>	<u>3,196,866</u>	<u>33,414,835</u>	<u>31,711,250</u>	<u>2,766,409</u>	<u>34,477,659</u>	<u>31,168,280</u>	<u>2,757,348</u>	<u>33,925,628</u>			
Total net assets – ending	<u>\$31,711,250</u>	<u>\$2,766,409</u>	<u>\$34,477,659</u>	<u>\$31,864,002</u>	<u>\$2,757,348</u>	<u>\$34,621,350</u>	<u>\$31,434,462</u>	<u>\$3,271,279</u>	<u>\$34,705,741</u>			

(1) The City implemented GASB Statement No. 34 beginning with its financial statements for fiscal year 2002-03, therefore numbers presented for fiscal years 2000-01 through 2001-02 may not be directly comparable to those for fiscal years 2002-03 and 2003-04.

Source: City of Morgan Hill audited financial statements for fiscal years 2000-01 through 2003-04.

Long Term Obligations

Upon issuance of the Bonds, long-term obligations payable out of the Water Revenue Fund will include the 1999 Installment Payments, the 2003 Loan and the Installment Payments. At September 30, 2004, the aggregate remaining outstanding principal amounts of the 1999 Installment Payments and the 2003 Loan were \$4,360,000 and \$1,470,437, respectively. The final 1999 Installment Payment is due June 1, 2021 and the final principal payment date for the 2003 Loan is June 1, 2017; provided, that in either case, the City may exercise the option to make prepayments pursuant to the related agreements. The City may, from time to time, incur additional indebtedness ranked on a parity with the Installment Payments, subject to the conditions set forth in the Installment Sale Agreement. See “SECURITY FOR THE BONDS –Additional Obligations Payable from Net Revenues.”

Debt Service Coverage

The table below sets forth the historical and projected Water System debt service coverage for fiscal years 1998-99 through 2006-07. The projections are based on the City’s current expectations and are subject to a number of factors and uncertainties that could cause actual results of operations and funds available for debt service to differ materially from those set forth herein.

Table 10
CITY OF MORGAN HILL
Historical and Projected Debt Service Coverage
Fiscal Years 2004-05 through 2008-09

Fiscal Year ⁽¹⁾	Gross Revenues ⁽¹⁾	Oper. & Mainten. Costs ⁽²⁾	Available Revenues ⁽³⁾	Debt Service			Total	Debt Service Coverage ^{(6)*}
				1991/1999 Installment Payments ⁽⁴⁾	Prior State Loan/ 2003 Loan ⁽⁵⁾	2004 Installment Payments*		
1999	\$5,938,444	\$3,088,856	\$2,849,588	\$385,750	\$166,007	\$ --	\$551,757	5.16
2000	6,057,670	3,060,729	2,996,941	356,135	166,007	--	522,142	5.74
2001	6,511,142	3,732,717	2,778,425	382,433	166,007	--	548,440	5.07
2002	6,119,826	4,144,657	1,975,169	381,433	166,008	--	547,441	3.61
2003	6,347,072	4,680,507	1,666,565	380,233	166,008	--	546,241	3.05
2004	7,221,814	5,027,029	2,194,785	378,827	157,497	--	536,324	4.09
2005 ⁽⁷⁾	7,300,000	5,608,794	1,691,206	382,233	148,388	201,828	732,449	2.31
2006 ⁽⁷⁾	7,573,560	5,898,408	1,584,152	385,233	148,388	341,063	874,684	1.81
2007 ⁽⁷⁾	7,858,016	6,477,590	1,380,426	382,832	148,388	341,063	872,283	1.58

(1) Pursuant to definition of "Gross Revenues" set forth in the Installment Sale Agreement, excludes revenues from perchlorate surcharge, which are to be used solely for perchlorate-related costs. See "THE WATER SYSTEM – Rates, Charges and Fees – Perchlorate Surcharge" and "– Environmental Issues – Perchlorate."

(2) Pursuant to the definition of "Operations and Maintenance Costs" set forth in the Installment Sale Agreement, excludes perchlorate-related costs, to the extent that such costs are covered by revenues from the perchlorate surcharge.

(3) Equals operating revenues minus operating and maintenance costs.

(4) Proceeds from the 1999 Certificates were used to refund certain certificates of participation executed and delivered in 1991.

(5) Proceeds from the 2003 Loan were used to refinance a prior State loan.

(6) Equals available revenues divided by sum of debt service for the 1999 Installment Payments, the 2003 Loan and the Installment Payments.

(7) Projected.

Source: Revenues and operation and maintenance costs from City of Morgan Hill; projected debt service amounts and coverage from RBC Dain Rauscher Inc.

THE AUTHORITY

The Authority was established pursuant to Article 1 (commencing with Section 6500) of Chapter 5, Division 7, Title 1 of the California Government Code and a Joint Exercise of Powers Agreement, dated as of November 5, 2003, by and between the City and the Morgan Hill Redevelopment Agency. The governing board of the Authority is the Authority Commission and is comprised of all of the individuals who currently are members of the City Council of the City. The Authority is qualified to assist in the financing of certain public improvements and to issue the Bonds under the Bond Law. The Authority has no taxing power. The Authority and the City are each separate and distinct legal entities, and the debts and obligations of each such entity are not debts or obligations of the other entity.

BONDOWNERS' RISKS

INVESTMENT IN THE BONDS INVOLVES ELEMENTS OF RISK. THE FOLLOWING SECTION DESCRIBES CERTAIN SPECIFIC RISK FACTORS AFFECTING THE PAYMENT AND SECURITY OF THE BONDS. THE FOLLOWING DISCUSSION OF RISKS IS NOT MEANT TO BE AN EXHAUSTIVE LIST OF THE RISKS ASSOCIATED WITH THE PURCHASE OF THE BONDS AND THE ORDER OF DISCUSSION OF SUCH RISKS DOES NOT NECESSARILY REFLECT THE RELATIVE IMPORTANCE OF THE VARIOUS RISKS.

* Preliminary; subject to change.

POTENTIAL INVESTORS ARE ADVISED TO CONSIDER THE FOLLOWING FACTORS ALONG WITH ALL OTHER INFORMATION IN THIS OFFICIAL STATEMENT IN EVALUATING THE BONDS. THERE CAN BE NO ASSURANCE THAT OTHER RISK FACTORS NOT DISCUSSED UNDER THIS CAPTION WILL NOT BECOME MATERIAL IN THE FUTURE.

Limited Obligations with Respect to the Bonds

The Bonds are limited obligations of the Authority payable solely from, and secured by, a pledge of Revenues and certain funds and accounts held under the Trust Agreement. Revenues consist primarily of Installment Payments payable by the City under the Installment Sale Agreement. If, for any reason, the Revenues collected under the Installment Sale Agreement are not sufficient to pay debt service on the Bonds, the Authority will not be obligated to utilize any other of its funds, other than moneys on deposit in the Reserve Account and certain other funds and accounts established under the Trust Agreement, to pay debt service on the Bonds. The Authority has no taxing power. The obligation of the City to make Installment Payments is a special obligation limited solely to Net Revenues of the Water System. No other funds or property of the City will be liable for the payment of the Installment Payments or any other amounts payable under the Installment Sale Agreement or the Trust Agreement. The Installment Payments do not constitute an obligation of the City which the City is obligated to levy or pledge any form of taxation or for which the City has levied or pledged any form of taxation.

System Operation and Expenses; Net Revenues

Projected revenues, operational expenses and demands of the Water System described in this Official Statement are based on certain assumptions which the City believes are reasonable. However, no assurance can be given that actual operating results will be consistent with these projections. The Water System's Net Revenues may be affected by the disruption in service from system failures, a lack of development, the relocation out of the Service Area, or the discontinued use of the City's water service, by one or more major customers, an increase in water supply costs or other operating costs of the Water System, or a number of other risks factors, whether or not described herein. The occurrence of any of these events, or changes in technology or regulatory standards, could impact the Water System's revenues and expenses. In such case, the City may be required to increase its water rates and charges in order to comply with the City's rate covenant under the Installment Sale Agreement. Under certain circumstances, Net Revenues may be affected to the extent that the City may be unable, as a practical matter, to raise rates in accordance with the rate covenant. See, for example, "CONSTITUTIONAL PROVISIONS AFFECTING WATER SYSTEM REVENUES AND EXPENDITURES." Receipt of the Water System's Net Revenues in amounts sufficient to pay Installment Payments is dependent on the continual use of utilities at forecasted levels.

Environmental Regulations; Maintenance of Water Quality Standards

The operation of the Water System is subject to state and federal laws and regulations, particularly with respect to water quality requirements. The City believes that it is in compliance with all state and federal drinking water quality standards. The adoption of more stringent laws and regulations may cause the City to incur greater expenses for the operation of the Water System, particularly, for example, if such change requires the use of new or costly technology. Although the City covenants in the Installment Sale Agreement to fix rates and collect revenues for the Water System to meet certain debt service coverage requirements (see "SECURITY FOR THE BONDS – Rate Covenant"), no assurance can be given that the costs of complying with such new laws and regulations will not adversely affect the City's ability to generate sufficient Net Revenues in the amounts required by the Installment Sale Agreement. It is not possible to predict the timing or nature of more stringent operation standards that may be imposed on the City over the terms of the Bonds.

As discussed in “THE WATER SYSTEM – Environmental Issues,” the contaminant perchlorate has been discovered in the City’s groundwater wells, leading to the permanent closing of one well and the temporary closing of two other wells. The City has taken, and continues to take, various actions relating to testing, clean-ups and monitoring in response to such discovery. The City Council, by adopting Resolution No. 5766, approved a surcharge in addition to the monthly water commodity and service charges in an effort to cover the unexpected costs incurred because of the perchlorate contamination. See “THE WATER SYSTEM – Rates, Charges and Fees – *Perchlorate Cost* Surcharge.” In the event that revenues from the surcharge prescribed by Resolution No. 5766 prove to be insufficient in covering all of the City’s perchlorate-related costs, the City may be required to increase rates to further recover the additional costs and to comply with its rate covenant under the Installment Sale Agreement. In the City’s continuing effort to comply with state and federal laws, regulations and guidelines and to maintain the standard of its water supply, unexpected costs may arise from time to time. Such unexpected costs, if significant, may adversely affect the amount of Net Revenues available to pay Installment Payments when due.

Natural Calamities; Earthquakes; Disasters

From time to time, the City is subject to natural calamities that may adversely affect economic activity in the City. The City, like most communities in California, is an area of unpredictable seismic activity, and therefore, is subject to potentially destructive earthquakes. The occurrence of a natural calamity, such as an earthquake or a drought, or any other disaster, may affect the City’s water supply, substantially damage or destroy Water System facilities or otherwise disrupt Water System operation. In such circumstances, Net Revenues may be reduced or eliminated if the City was unable to provide water services to its customers, or if large amounts of revenues were required to be applied to make extensive repairs to the Water System. Such a reduction or elimination of Net Revenues could impair the City’s ability to make Installments Payments when due.

Additional Obligations of the City

The Installment Sale Agreement permit the incurrence of additional obligations secured by Net Revenues on a parity basis to the Installment Payments, upon the City’s compliance with certain conditions. See “SECURITY FOR THE BONDS – Additional Obligations Payable from Net Revenues.” The City anticipates incurring Additional Parity Obligations in the future. Such Additional Parity Obligations would increase debt service payable from Net Revenues and could adversely debt service coverage debt service coverage with respect to the Installment Payments. In such event, however, the rate covenant of the City under the Installment Sale Agreement will remain in effect. See “SECURITY FOR THE BONDS – Rate Covenant.”

Limitations on Remedies

Remedies available to the Owners may be limited by a variety of factors and may be inadequate to assure the timely payment of principal of and interest and premium, if any, on the Bonds or to preserve the tax-exempt status of interest on the Bonds.

Bond Counsel has limited its opinion as to the enforceability of the Bonds and the Trust Agreement and the Installment Sale Agreement to the extent that enforceability may be limited by bankruptcy, insolvency, reorganization, fraudulent conveyance or transfer, moratorium, or others similar laws affecting generally the enforcement of creditor’s rights, by equitable principles and by the exercise of judicial discretion. Additionally, the Bonds are not subject to acceleration in the event of the breach of any covenant or duty under the Trust Agreement. The lack of availability of certain remedies or the limitation of remedies may entail risks of delay in the exercise of, or limitations on or modifications to,

the rights of the Owners.

Enforceability of the rights and remedies of the owners of the Bonds, and the obligations incurred by the Authority, may become subject to the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or affecting the enforcement of creditor's rights generally, now or hereafter in effect, equity principles which may limit the specific enforcement under State law of certain remedies, the exercise by the United States of America of the powers delegated to it by the Constitution, the reasonable and necessary exercise, in certain exceptional situations, of the police powers inherent in the sovereignty of the State and its governmental bodies in the interest of serving a significant and legitimate public purpose and the limitations on remedies against governmental entities in the State.

Investment of Funds

The Reserve Account and all other funds held under the Trust Agreement are required to be invested in Permitted Investments as provided under the Trust Agreement, respectively. See "APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS." All investments, including Permitted Investments, authorized by law from time to time for investments by the Authority contain a certain degree of risk. Such risks include, but are not limited to, a lower rate of return than expected, decline in market value and loss or delayed receipt of principal. The occurrence of these events with respect to amounts held under the Trust Agreement could have a material adverse effect on the security for the Bonds.

Constitutional Limitations; Future Initiative and Legislation

As discussed herein under "CONSTITUTIONAL PROVISIONS AFFECTING WATER SYSTEM REVENUES AND EXPENDITURES," the California's Constitutional initiative process has resulted in the adoption of measures which pose certain limits on the ability of cities and local agencies to generate revenues, through property taxes or otherwise. From time to time, other initiative measures could be adopted, affecting the City's ability to generate revenues and to increase appropriations. No assurances can be given as to the potential impact of any future initiative or legislation on the finances and operations of the City.

Loss of Tax Exemption

In order to maintain the exclusion from gross income for federal income tax purposes of the interest on the Bonds, the Authority and the City have covenanted to comply with the applicable requirements of Section 148 and certain other sections of the Internal Revenue Code of 1986, as amended, relative to arbitrage and avoidance of characterization as private activity bonds, among other things. The interest on the Bonds could become includable in gross income for purposes of federal income taxation retroactive to the date of issuance of the Bonds as a result of acts or omissions of the Authority and/or the City in violation of their covenants. Should such an event of taxability occur, the Bonds are not subject to acceleration, redemption or any increase in interest rates and will remain Outstanding until maturity or until redeemed under one of the redemption provisions contained in the Trust Agreement. See "TAX MATTERS."

Secondary Market

There can be no assurance that there will be a secondary market for the Bonds, or if a secondary market exists, that such Bonds can be sold for any particular price. Occasionally, because of general market conditions or because of adverse history or economic prospects connected with a particular issue,

secondary marketing practices in connection with a particular issue are suspended or terminated. Additionally, pricing of issues for which a market is being made will depend upon then prevailing circumstances. Such prices could substantially differ from the original purchase price.

CONSTITUTIONAL PROVISIONS AFFECTING WATER SYSTEM REVENUES AND EXPENDITURES

Article XIII A and Article XIII B

Pursuant to California law, any fee that exceeds the reasonable cost of providing the service for which the fee is charged is a “special tax,” which under Article XIII A of the California Constitution must be authorized by a two-thirds vote of the electorate. This requirement may be applicable to rates for water service and capacity charges, to the extent that such rates and charges exceed the reasonable costs of providing service. In addition, the California courts have determined that fees such as connection fees (capacity charges) will not be special taxes if they approximate the reasonable cost of constructing the water system improvements contemplated by the local agency imposing the fee. Such court determinations have been codified in California Government Code Section 66005.

On November 6, 1979, California voters approved Proposition 4, the “Gann Initiative,” which added Article XIII B to the California Constitution. Under Article XIII B, state and local governmental entities have an annual “appropriations limit” and are not permitted to spend certain moneys that are called “appropriations subject to limitation” (consisting of tax revenues, state subventions, and certain other funds) in an amount higher than the “appropriations limit.” Article XIII B does not affect the appropriations of moneys that are excluded from the definition of “appropriations subject to limitation,” including debt service on indebtedness existing or authorized as of January 1, 1979, or bonded indebtedness subsequently approved by the voters. In general terms, the “appropriations limit” is to be based on certain 1978-79 expenditures and is to be adjusted annually to reflect changes in consumer prices, populations, and services provided by these entities. Among other provisions of Article XIII B, if these entities’ revenues in any tax year exceed the amounts permitted to be spent, the excess would have to be returned by revising tax rates or fee schedules over the subsequent two years. Certain expenditures are excluded from the appropriation limit, including payments of indebtedness existing or legally authorized as of January 1, 1979, or of bonded indebtedness thereafter approved by voters and payments required to comply with court or federal mandates which without discretion required an expenditure for additional services or which unavoidably make the providing of existing services more costly.

The City believes that its rates and charges for water service do not exceed the costs the City reasonably bears in providing existing such services, and is presently in compliance with Article XIII A and Article XIII B.

Proposition 218: Article XIII C and Article XIII D

General. On November 5, 1996, California voters approved Proposition 218, “the Right to Vote on Taxes Act.” Proposition 218 added Articles XIII C and XIII D to the California Constitution, providing certain vote requirements and other limitations on the imposition of new or increased taxes, assessments, and property-related fees and charges.

Article XIII C. Article XIII C provides that a local government may not impose, extend, or increase local taxes until such taxes are submitted to the electorate for approval. General taxes, imposed, extended, or increased for general governmental purposes of the city, require a majority vote and special taxes, imposed, extended, or increased for specific purposes, require a two-thirds vote. In addition, Article XIII C provides that the constitutional initiative power shall not be prohibited or otherwise limited

in matters of reducing or repealing any local taxes, assessments, fees, and charges. This provision with respect to the initiative power is not limited to taxes, assessments, fees, and charges imposed on or after November 6, 1996, the effective date of Proposition 218. However, on July 1, 1997, a bill was signed into law by the Governor of the State enacting Government Code Section 5854, which states: "Section 3 of Article XIIC of the California Constitution, as adopted at the November 5, 1996 general election, shall not be construed to mean that any owner or beneficial owner of a municipal security, purchased before or after that date, assumes the risk of, or in any way consents to, any action by initiative measure that constitutes an impairment of contractual rights protection by Section 10 of Article I of the United States Constitution." Government Code Section 5854 appears to limit the voters' power to repeal or reduce Water System fees and charges if such reduction would interfere with the City's payment of Installment Payments. If Government Code Section 5854 becomes the subject of a challenge, however, no guarantee can be made that the courts will agree with such interpretation.

Article XIID. Article XIID imposes various procedural and substantive requirements on local governments that levy an "assessment," "fee," or "charge." An assessment is defined as any levy or charge upon real property by an agency for a special benefit conferred upon real property. A fee or charge is defined as "any levy other than an *ad valorem* tax, a special tax, or an assessment, imposed by a local government upon a parcel or upon a person merely as an incident of property ownership, including user fees or charges for a property related service." Under Section 6 of Article XIID, a fee or charge (i) may not exceed the funds required to provide the "property related service," (ii) may not be used for any purpose other than that for which the fee or charge was imposed, (iii) may not exceed the proportional cost of the service attributable to the parcel, (iv) may not be imposed for a service unless that service is actually used by, or is immediately available to, the owner of the property in question, and (v) may not be imposed for general governmental services where the service is "available to the public at large in substantially the same manner as it is to property owners." In addition, before any property related fee or charge may be imposed or increased, written notice must be given to the record owner of each parcel of land affected by such fee or charge. The local government agency must then hold a hearing upon the proposed imposition or increase, and if written protests against the proposal are presented by a majority of the owners of the identified parcels, the local government agency may not impose or increase the fee or charge. Moreover, except for fees or charges for water, wastewater, and refuse collection services (or fees for electrical and gas service, which are expressly exempted from Proposition 218), no property related fee or charge may be imposed or increased without a majority approval by the property owners subject to the fee or charge or, at the option of the local agency, two-thirds approval by those residing in the affected area and voting at the election.

Water Service Fees and Charges. Since the enactment of Proposition 218 in 1996, local governments have been made different interpretations as to whether water service fees and charges are property related fees and charges subject to the requirements of Section 6 of Article XIID. The California Supreme Court's decision in *Richmond v. Shasta Community Services District* (published February 9, 2004) addressed the applicability of Article XIID to water service fees and charges but did not completely resolve the uncertainty. In *Richmond*, the Shasta Community Services District charged a water connection fee that included a capacity charge for capital improvements to the Water System and a fire suppression charge. The Court held that both the capacity charge and the fire suppression charge were not subject to Article XIID because the water connection fee is neither an assessment nor a property related fee or charge since the water connection fee results from property owners' voluntary decision to apply for the connection. In a discussion not essential to the holding, however, the Court stated that a fee for existing water service through an existing water connection that requires nothing other than normal ownership and use of the property is a property related fee or charge. As a result, the Court suggests that a fee or charge for existing water service through an existing water connection must comply with the requirements of Section 6 of Article XIID.

The City has taken the position that its water charges are not fees or charges imposed as an incident of property ownership within the meaning of Article XIID. As the interpretation and application of Proposition 218 to water charges may be ultimately determined by the courts, it is not possible to predict with certainty the outcome of such determination. If the limitations of Article XIID are held to be applicable, it is possible that a court may find the City's water charges to not be in compliance.

Future Initiatives

Articles XIII A, XIII B, XIII C and XIID of the California Constitution were each adopted as measures that qualified for the ballot pursuant to the State's initiative process. From time to time, other initiative measures could be adopted, further affecting the Water System revenues or the City's ability to expend such revenues.

ABSENCE OF LITIGATION

To the Authority's and the City's knowledge, there is no litigation pending or threatened to restrain or enjoin the issuance, execution or delivery of the Bonds, to contest the validity of the Bonds or any proceedings of the City or the Authority with respect thereto. In the opinion of the Authority and its counsel, there is no lawsuit or claim pending against the Authority which will materially impair the Authority's ability to enter into the Trust Agreement or restrain or enjoin the collection of Revenues as contemplated therein. In the opinion of the City and its City Attorney, there is no lawsuit or claim pending against the City which will materially impair the City's ability to enter into the Installment Sale Agreement or restrain or enjoin the collection of Net Revenues to pay Installment Payments as contemplated in therein.

CONTINUING DISCLOSURE

Pursuant to Rule 15c2-12 of the Securities and Exchange Commission (the "Rule"), the City has entered into an agreement with BNY Western Trust Company, as Trustee and Dissemination Agent (the "Dissemination Agent"), for the benefit of holders of the Bonds to provide certain financial information and operating data relating to the City and the balances of funds relating to the Bonds, by not later than February 15 of each Fiscal Year commencing with the report for the 2004-05 fiscal year (the "Annual Information"), and to provide notices of the occurrence of certain enumerated events, if deemed by the City to be material. The Annual Information will be filed by the Dissemination Agent, with each Nationally Recognized Municipal Securities Information Repository (the "NRMSIRS") and with the State Information Depository (the "State Depository"), if any. Notices of material events will be filed by or on behalf of the City with the NRMSIRS or the Municipal Securities Rulemaking Board (the "MSRB") and with the State Depository, if any. The nature of the information to be provided in the Annual Information and the notices of material events is set forth under the caption "APPENDIX E – FORM OF CONTINUING DISCLOSURE AGREEMENT." Except for one prior instance (which has since been cured), the City has met all of its filing requirements under other similar continuing disclosure certificates or agreements.

LEGAL MATTERS

The legality of the issuance of the Bonds is subject to the approval of Richards, Watson & Gershon, A Professional Corporation, Los Angeles, California, Bond Counsel. Bond Counsel's opinions with respect to the Bonds will be substantially in the forms set forth in APPENDIX D of this Official Statement. Fees payable to Bond Counsel are contingent upon successful sale and delivery of the Bonds.

TAX MATTERS

In the opinion of Richards, Watson & Gershon, A Professional Corporation, Bond Counsel, under existing law interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the “Code”), and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. Bond Counsel will express no opinion as to any other federal tax consequences regarding the Bonds.

The opinion on federal tax matters will be based on and will assume the accuracy of certain representations and certifications, and continuing compliance with certain covenants, of the Authority and the City that are intended to assure the foregoing, including that the Bonds are and will remain obligations the interest on which is excluded from gross income for federal income tax purposes. Bond Counsel will not independently verify the accuracy of those representations and certifications.

The Code prescribes a number of qualifications and conditions for the interest on state and local government obligations to be and to remain excluded from gross income for federal income tax purposes. Some of these qualifications and conditions require future or continued compliance after issuance of the obligations for the interest to be and to continue to be excluded from the date of issuance. Noncompliance with these qualifications and conditions by the Authority or the City may cause the interest on the Bonds to be included in gross income for federal income tax purposes retroactively to the date of issuance of the Bonds. The Authority and the City have covenanted to take the actions required of it for the interest on the Bonds to be and to remain excluded from gross income for federal income tax purposes, and not to take any actions that would adversely affect that exclusion.

Under the Code, a portion of the interest on the Bonds earned by certain corporations may be subject to a corporate alternative minimum tax. In addition, interest on the Bonds may be subject to a branch profits tax imposed on certain foreign corporations doing business in the United States and to a tax imposed on excess net passive income of certain S corporations.

Under the Code, the exclusion of interest from gross income for federal income tax purposes may have certain adverse federal income tax consequences on items of income, deduction or credit for certain taxpayers, including financial institutions, certain insurance companies, recipients of Social Security and Railroad Retirement benefits, those that are deemed to incur or continue indebtedness to acquire or carry tax-exempt obligations, and individuals otherwise eligible for the earned income tax credit. The applicability and extent of these and other tax consequences will depend upon the particular tax status or other tax items of the owners of the Bonds. Bond Counsel will express no opinion regarding those consequences.

Any excess of the stated redemption price at maturity of the Bonds over the initial offering price to the public of the Bonds set forth on the inside cover of this Official Statement is “original issue discount.” Such original issue discount accruing on a Bond is treated as interest excluded from the gross income of the owner thereof for federal income tax purposes and exempt from California personal income tax. Original issue discount on any Bond purchased at such initial offering price and pursuant to such initial offering will accrue on a semiannual basis over the term of the Bond on the basis of a constant yield method and, within each semiannual period, will accrue on a ratable daily basis. The amount of original issue discount on such a Bond accruing during each period is added to the adjusted basis of such Bond to determine taxable gain upon disposition (including sale, redemption or payment on maturity) of such Bond. The Code includes certain provisions relating to the accrual of original issue discount in the case of purchasers of the Bonds who purchase the Bonds other than at the initial offering price and pursuant to the initial offering. Any person considering purchasing a Bond should consult his or her own tax advisors with respect to the tax consequences of ownership of bonds with original issue discount,

including the treatment of purchasers who do not purchase in the original offering and the original offering price, the allowance of a deduction for any loss on a sale or other disposition, and the treatment of accrued original issue discount on such bonds under federal individual and corporate alternative minimum taxes.

If the Bonds were offered and sold to the public at a price in excess of their stated redemption price (the principal amount) at maturity, that excess constitutes “premium.” For federal income tax purposes, that premium is amortized over the period to maturity of the Bonds, based on the yield to maturity of the Bonds, compounded semiannually. No portion of that premium is deductible by the owner of a Bond. For purposes of determining the owner’s gain or loss on the sale, redemption (including redemption at maturity) or other disposition of a Bond, the owner’s tax basis in the Bond is reduced by the amount of premium that accrues during the period of ownership. As a result, an owner may realize taxable gain for federal income tax purposes from the sale or other disposition of a Bond for an amount equal to or less than the amount paid by the owner for that Bond. A purchaser of a Bond in the initial public offering at the price for that Bond stated on the cover of this Official Statement who holds that Bond to maturity will realize no gain or loss upon the retirement of that Bond. Owners of the Bonds should consult their own tax advisers as to the determination for federal income tax purposes of the amount of premium properly accruable in any period with respect to the Bonds and as to other federal tax consequences and the treatment of premium for purposes of state and local taxes on, or based on, income.

Purchasers of the Bonds at other than their original issuance at the respective prices indicated on the cover of this Official Statement should consult their own tax advisers regarding other tax considerations such as the consequences of market discount.

A copy of the proposed form of opinion of Bond Counsel is attached hereto as APPENDIX D.

FINANCIAL ADVISOR

RBC Dain Rauscher Inc. has acted as financial advisor to the Authority concerning the Bonds. As financial advisor, RBC Dain Rauscher Inc. will receive compensation contingent upon the sale and delivery of the Bonds.

UNDERWRITING

The Authority has awarded the Bonds to _____ (the “Underwriter”) in a competitive sale held on _____, 2004. The Underwriter has agreed, subject to certain conditions, to purchase the Bonds at a purchase price of \$_____, which includes a net original issue [discount/premium] of \$_____ and an underwriter’s discount of \$_____. The Underwriter intends to offer the Bonds to the public initially at the prices set forth on the inside cover page of this Official Statement, which prices may subsequently change without any requirement of prior notice.

RATINGS

Standard & Poor’s (“S&P”) and Moody’s Investors Service (“Moody’s”) have assigned ratings of “AAA” and “Aaa,” respectively, to the Bonds, conditioned on the issuance by the Bond Insurer of the Bond Insurance Policy at the time of delivery of the Bonds. The Authority has not applied to any rating agency for the assignment of an underlying rating for the Bonds. The ratings assigned by the rating agencies reflect only the views of such organizations and any desired explanation of the significance of such ratings may be obtained from S&P and Moody’s. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance such ratings will continue for any given period of time or that such ratings will not be

revised downward or withdrawn entirely by the rating agencies, if in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Bonds.

MISCELLANEOUS

All of the preceding description and summaries of the Bonds, the Trust Agreement, the Installment Sale Agreement, other applicable agreements, legislation and other documents are made subject to the provisions of such documents respectively and do not purport to be complete statements of any or all of such provisions. Reference is hereby made to such documents on file with the City for further information.

Any statements made in this Official Statement involving matters of opinion or of estimates, whether or not so expressly stated, are set forth as such and not as representations of fact, and no representation is made that any of the estimates will be realized.

The Authority and the City have duly authorized the execution and delivery of this Official Statement by their authorized officers.

MORGAN HILL FINANCING AUTHORITY

By: _____
Chief Administrative Officer

CITY OF MORGAN HILL

By: _____
City Manager

APPENDIX A

SUPPLEMENTAL INFORMATION ABOUT THE CITY OF MORGAN HILL

This Appendix is included solely to provide background and demographic information regarding the City of Morgan Hill. The City's obligation to pay Installment Payments is a special obligation limited solely to the Net Revenues of the Water System. No other funds or property of the City shall be liable for the payment of the Installment Payments or any other amounts payable under the Installment Sale Agreement or the Trust Agreement.

General

The City of Morgan Hill (the "City") is located against the foothills of the Coastal Ranges near the southern end of the Santa Clara Valley in the southern part of the Santa Clara County (the "County"). The City is located 70 miles south of San Francisco and 20 miles south of San Jose. The City is bordered by San Martin and Gilroy to the south, San Jose to the north, and unincorporated county land to the east and west. The City encompasses an area of approximately 11 square miles with an average elevation of 345 feet above sea level.

Incorporated on November 10, 1906 as a general law city, the City currently functions under a Council/Manager form of Government. A five member City Council, including the Mayor, is elected at large. The City Treasurer and the City Clerk are also elected at large. The City currently employs approximately 156 permanent employees.

The current members of the City Council are as follows:

<u>Name and Office</u>	<u>Current Term Expires</u>
Dennis Kennedy, <i>Mayor</i>	November 2004
Greg Sellers, <i>Mayor Pro Tem</i>	November 2006
Larry Carr, <i>Council Member</i>	November 2004
Hedy L. Chang, <i>Council Member</i>	November 2004
Steve Tate, <i>Council Member</i>	November 2006

Population

The City's population was approximately 35,500 as of January 1, 2004, according to the California State Department of Finance's estimates. The table below shows the population growth in the City and the County from January 1, 1995 through January 1, 2004:

CITY OF MORGAN HILL
City and County Population
Calendar Years 1995 through 2004

	<u>City</u>	
<u>Year ⁽¹⁾</u>	<u>Population</u>	<u>Growth Rate</u>
1995	27,138	3.05%
1996	28,100	4.07
1997	29,300	4.27
1998	30,750	4.95
1999	31,850	3.58
2000	33,200	4.24
2001	34,250	3.16
2002	34,750	1.46
2003	34,750	0.00
2004	35,500	2.16

⁽¹⁾ As of January 1 of each year.

Source: State of California, Department of Finance, Demographic Research Unit

Residential Development Control System. A voter-approved growth management system, known as the Residential Development Control System (“RDSCS”), was enacted by the City’s voters in 1977, as Measure E. It was later updated in 1990, as Measure P, and in March 2004, as Measure C. Measure C, among other things, extended the expiration of the RDSCS through the end of fiscal year 2020. The RDSCS is embodied in Chapter 18.78 of the City’s Municipal Code, as well as the City’s General Plan and Zoning Ordinance. Generally, the RDSCS regulates growth by limiting the number of new homes to be built each year, according to a point system based on a variety of factors including provision of public services, site planning and architectural design considerations. Measure C establishes a population ceiling of 48,000 in the City through the end of fiscal year 2020. Measure C may not be amended except by another public vote.

Employment

According to the State of California Employment Development Department, the City’s preliminary, estimated unemployment rate for July 2004 was 4.9 percent. The following table shows certain employment statistics for the City and the County for calendar years 1994 through 2003.

CITY OF MORGAN HILL
City and County Employment Statistics
Calendar Years 1994 through 2003 ⁽¹⁾

Year	City			County
	Labor Force	Employed	Unemployment Rate	Unemployment Rate
1994	12,850	12,220	4.9%	6.2%
1995	12,960	12,460	3.9	4.9
1996	13,460	13,080	2.8	3.6
1997	14,100	13,770	2.4	3.0
1998	14,390	14,030	2.5	3.2
1999	14,480	14,140	2.4	3.0
2000	15,190	14,960	1.5	2.0
2001	15,070	14,530	3.6	4.6
2002	14,130	13,180	6.7	8.5
2003	13,410	12,540	6.5	8.2

⁽¹⁾ Figures represent the 12-month average for each such year.

Source: State of California, Employment Development Department.

The following table lists the major area employers in the City.

CITY OF MORGAN HILL
Major Area Employers
as of September 30, 2004

<u>Company</u>	<u>Product/Service</u>	<u>Full-Time Employees</u>
Morgan Hill Unified School District	Education	866
Hospira Inc.	Electronic hospital products	565
Anritsu Company	Microwave testing equipment	485
Comcast Cable Communications	Cable provider	355
Safeway	Grocery store	324
Fox Racing	Off-road sports apparel manufacturer	306
E.D.O.	Electronic warfare systems	300
Paramit Corporation	Semiconductor manufacturing	243
The Thomas Kincaid Co.	Art marketing, products and sales	177
Target	Retail	146

Source: City of Morgan Hill.

Commerce; General Revenues

The table shows the dollar volume of taxable transactions in the City from 1998 through 2002:

CITY OF MORGAN HILL Taxable Transactions Calendar Years 1998 through 2002 (in Thousands of Dollars)

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>
Retail Outlets					
Apparel store	\$ 3,895	\$ 1,779	1,962	3,731	7,264
General merchandise stores	62,813	68,144	70,090	73,234	70,762
Food stores	21,819	22,566	23,892	24,531	23,831
Eating and drinking places	34,862	38,394	39,946	41,530	39,152
Home furnishing and appliances	8,547	9,793	13,417	11,470	9,996
Building materials and farm	11,060	10,506	9,321	7,874	6,320
Auto dealers and supplies	21,718	27,266	32,521	39,229	-- ⁽¹⁾
Service stations	25,227	30,141	34,763	33,375	41,076
Other retail stores	<u>54,582</u>	<u>59,995</u>	<u>65,523</u>	<u>61,322</u>	<u>99,549</u> ⁽¹⁾
Subtotal	244,523	268,584	291,435	296,296	297,950
All Other Outlets	<u>83,433</u>	<u>107,979</u>	<u>148,507</u>	<u>153,486</u>	<u>100,118</u>
All Outlets	<u>\$327,956</u>	<u>\$376,563</u>	<u>\$439,942</u>	<u>\$449,782</u>	<u>\$398,068</u>

⁽¹⁾ Figure omitted because its publication would result in the disclosure of confidential information. To the extent possible, sales are included in "Other retail stores."

Source: State of California, Board of Equalization.

The following table presents the City's general governmental revenues, categorized by source, from fiscal years 1999 through 2003.

CITY OF MORGAN HILL City General Governmental Revenue Fiscal Years 1999 through 2004

<u>Fiscal Year</u>	<u>Property Tax</u>	<u>Sales Taxes</u>	<u>Franchise, Hotel and Other Taxes</u>	<u>Funding from Other Gov'ts</u>	<u>License Service Charges</u>	<u>Interest Fines and Other</u>	<u>Total</u>
1999	\$15,049,473	\$3,990,716	\$1,994,321	\$2,471,349	\$7,127,820	\$5,059,442	\$35,693,121
2000	17,655,775	4,454,774	2,525,798	3,000,557	5,033,724	4,441,596	37,112,224
2001	18,431,805	5,532,132	2,803,261	6,628,611	8,032,803	6,498,641	47,927,253
2002	19,454,298	4,870,295	2,443,461	3,316,144	6,769,058	4,947,817	41,801,073
2003	24,226,642	4,636,927	2,401,341	3,140,343	7,585,951	3,223,115	45,214,319
2004 *	24,932,255	4,070,030	3,154,457	2,832,786	9,352,727	6,918,920	51,261,175

* Unaudited

Source: City of Morgan Hill Annual Financial Reports.

Assessed Value and Construction Activity

The following is a summary of aggregate assessed value of properties in the City and construction permits issued by the City from fiscal years 1999-00 through 2003-04.

CITY OF MORGAN HILL **Assessed Value, Building Permits Issued and Values for Permits Issued** **Fiscal Years 1999-00 through 2003-04**

Fiscal Year	Aggregate Assessed Value	Building Permits	<u>Value of Permits Issued</u>		
			<u>Commercial</u>	<u>Residential</u>	<u>Total</u>
2000	\$2,906,464,530	1,312	\$31,214,390	\$45,608,507	\$76,822,897
2001	3,302,350,285	1,400	106,912,266	48,895,813	155,808,079
2002	3,724,450,362	1,457	22,044,283	73,537,055	95,581,338
2003	4,180,661,418	1,388	22,048,822	78,302,630	100,351,452
2004	4,489,930,909	1,407	36,876,375	84,488,801	121,364,476

Source: City of Morgan Hill, Building Department.

Utilities

Water is supplied by the City's Water Department. Sewage treatment and disposal is provided by the South County Regional Wastewater Authority. Pacific Gas & Electric Company provides natural gas and electric power to the City.

Transportation

The City is well served by area transportation routes. U.S. 101, a major north-south highway, bisects the City, linking the Santa Clara Valley with San Francisco, 70 miles to the north, and with Los Angeles, 380 miles to the South. U.S. 101 through the City is a six-lane freeway. The City also offers easy access to California 152, the east-west connecting route to Interstate 5, and California 156 over Hecker Pass to Watsonville and the coastal highway. Within 30 miles of the City are freeway interchanges with I-280 north to San Francisco, 880 to Oakland or Santa Cruz and I-680 to Sacramento.

Public transportation to the City includes Greyhound bus service and Santa Clara County Transit, with its dial-a-ride feature on selected routes. The City has been served by the Southern Pacific Railroad for over a century. Rail lines run through the City. Caltrain service through San Jose and the Peninsula to San Francisco began in 1992.

San Jose International Airport, 25 miles to the north, offers a full schedule of passenger and freight flights. Other airports within convenient access to the City include San Francisco International, Oakland International, and Monterey Airport. Three general aviation airports, providing general aviation facilities, are located in San Martin (five miles south), in Hollister (26 miles southeast), and in south San Jose (Reid Hillview, 15 miles north), respectively.

The City is 70 miles south of major deep water seaports at San Francisco and Oakland.

Climate

With a January average low temperature of 41 degrees Fahrenheit and a July average high temperature of 82 degrees Fahrenheit, the City enjoys comfortable weather throughout the year. Annual rainfall is about 14 inches, principally during the winter months. Winds are generally from the northwest

at a mean hourly speed of seven miles per hour. Its geographical setting protects the community from most smog.

Low humidity and an average of 345 days of sunshine provide a superb year round growing season for many crops. For years the City has been recognized as a leading agricultural center. Mushrooms, fresh fruits, nuts, prunes, and varietal wine grapes are the principal crops harvested in the area's fields and orchards.

APPENDIX B

EXCERPTS OF

CITY OF MORGAN HILL COMPREHENSIVE FINANCIAL REPORT

FOR YEAR ENDED JUNE 30, 2003

APPENDIX C
SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

APPENDIX D

FORM OF OPINION OF BOND COUNSEL

Upon issuance and delivery of the Bonds, Richards Watson & Gershon, A Professional Corporation, Bond Counsel, proposes to render its final approving opinion in substantially the following form:

[to come]

APPENDIX E

FORM OF CONTINUING DISCLOSURE AGREEMENT

This **Continuing Disclosure Agreement** (the “Disclosure Agreement”) is executed and delivered on this July 1, 2004, by the City of Morgan Hill (the “City”) and BNY Western Trust Company, in its capacities as Trustee (the “Trustee”) under the Trust Agreement (hereinafter defined) and Dissemination Agent, in connection with the issuance of \$_____ Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 (the “Bonds”).

The Bonds are being issued pursuant to a Trust Agreement, dated as of _____, 2004 (the “Trust Agreement”), by and between the Morgan Hill Financing Authority and the Trustee. Proceeds of the Bonds will be used by the Authority to provide funds for the City of Morgan Hill (the “City”) to finance certain improvements to the City’s Water System. The Bonds will be payable solely from Revenues and certain funds and accounts held under the Trust Agreement. Revenues consist primarily of Installment Payments payable by the City pursuant to an Installment Sale Agreement, dated as of _____, 2004, by and between the Authority and the City.

The City, the Trustee and the Dissemination Agent hereby covenant and agree as follows:

Section 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered for the benefit of the holders and beneficial owners of the Bonds and in order to assist the Participating Underwriter in complying with Securities and Exchange Commission Rule 15c2-12(b)(5).

Section 2. Definitions. In addition to the definitions set forth in the Trust Agreement and the Installment Sale Agreement, which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

“Annual Report” shall mean any Annual Report provided by the City pursuant to, and as described in, Sections 3 and 4 of this Disclosure Agreement.

“Disclosure Representative” shall mean the City Manager of the City or his or her designee, or such other person as the City shall designate in writing to the Trustee and the Dissemination Agent from time to time.

“Dissemination Agent” shall mean the BNY Western Trust Company, acting in its capacity as the Dissemination Agent hereunder or any successor Dissemination Agent designated in writing by the City and which has filed with the City and the Trustee a written acceptance of such designation.

“Listed Events” shall mean any of the events listed in Section 5(a) of this Disclosure Agreement.

“National Repository” shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule.

“Official Statement” shall mean the final Official Statement, dated June __, 2004, relating to the Bonds.

“Owners” shall mean the registered owners of the Bonds or, if the Bonds are registered in the name of a depository, the beneficial owners of the Bonds.

“Participating Underwriter” shall mean the original underwriter of the Bonds required to comply with the Rule in connection with offering of the Bonds.

“Repository” shall mean each National Repository and each State Repository.

“Rule” shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

“State Repository” shall mean any public or private repository or entity designated by the State of California as a state repository for the purpose of the Rule. As of the date of this Disclosure Agreement, there is no State Repository.

Section 3. Provision of Annual Reports.

(a) The City shall, or shall cause the Dissemination Agent to, not later than February 15 of each year, commencing with the report for the 2004-05 fiscal year, provide to each Repository an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Agreement, with a copy to the Trustee. Not later than fifteen (15) Business Days prior to said date, the City shall provide the Annual Report to the Dissemination Agent and the Trustee (if the Trustee is not the Dissemination Agent). The Annual Report may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in Section 4 of this Disclosure Agreement; provided that the audited financial statements of the City may be submitted separately from the balance of the Annual Report, and later than the date required above for the filing of the Annual Report if not available by that date. If the City’s fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(c) hereof. The City shall provide a written certification with each Annual Report furnished to the Dissemination Agent to the effect that such Annual Report constitutes the Annual Report required to be furnished by it hereunder. The Dissemination Agent may conclusively rely upon such certification of the City and shall have no duty or obligation to review such Annual Report.

(b) If within fifteen (15) Business Days prior to the date specified in subsection (a) for providing the Annual Report to the Repositories, the Dissemination Agent has not received a copy of the Annual Report, the Dissemination Agent shall contact the City to determine if the City is in compliance with subsection (a).

(c) If the Dissemination Agent is unable to verify that an Annual Report has been provided to the Repositories by the date required in subsection (a), the Dissemination Agent shall send a notice to that effect to the Municipal Securities Rulemaking Board in substantially the form attached hereto as Exhibit A.

(d) The Dissemination Agent shall:

(i) determine each year prior to the date for providing the Annual Report the name and address of each National Repository and each State Repository, if any, and

(ii) if the Annual Report has been furnished to the Dissemination Agent, file a report with the City and the Trustee (if the Dissemination Agent is not the Trustee)

certifying that the Annual Report has been provided pursuant to this Disclosure Agreement, stating the date it was provided and listing all the Repositories to which it was provided.

Section 4. Content of Annual Reports. The City's Annual Report shall contain or incorporate by reference the following:

(a) Audited Financial Statements of the City for the most recent fiscal year, prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board, and as further modified according to applicable State law. If the City's audited financial statements are not available at the time the Annual Report is required to be filed pursuant to Section 3(a) hereof, the Annual Report shall contain unaudited financial statements in a format similar to the usual format utilized by the City, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available;

(b) Updates of the information in Tables __, __ and __ of the Official Statement for the most recently ended fiscal year, in substantially the formats of such tables;

(c) The balance of Reserve Account as of the last day of the most recently ended fiscal year; and

(d) Principal amounts of the Bonds and all other outstanding Parity Obligations payable from Net Revenues as of the last day of the most recently ended fiscal year.

Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues of the City or related public entities, which have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The City shall clearly identify each such other document so included by reference.

Section 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the City shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

- (1) Principal and interest payment delinquencies;
- (2) Non-payment related defaults;
- (3) Unscheduled draws on debt service reserves reflecting financial difficulties;
- (4) Unscheduled draws on credit enhancements reflecting financial difficulties;
- (5) Substitution of credit or liquidity providers, or their failure to perform;
- (6) Adverse tax opinions or events affecting the tax-exempt status of the Bonds;
- (7) Modifications to rights of Bond Owners;
- (8) Optional, contingent or unscheduled Bond calls;
- (9) Defeasances;
- (10) Release, substitution, or sale of property securing repayment of the Bonds;
- (11) Rating changes.

(b) The Trustee shall, promptly upon obtaining actual knowledge of the occurrence of any of the Listed Events contact the Disclosure Representative, inform such person of the event, and request that the City promptly notify the Dissemination Agent in writing whether the Listed Event is material and, if so, whether or not to report the event pursuant to subsection (f), and promptly notify the Trustee in writing whether or not to report the event to the Owners (unless notice to the Owners is already required by the Trust Agreement). For purposes of this Disclosure Agreement, “actual knowledge” of the occurrence of such Listed Events shall mean actual knowledge by the officer at the Trust Office of the Trustee with regular responsibility for the administration of the Trust Agreement

(c) Whenever the City obtains knowledge of the occurrence of a Listed Event, whether because of a notice from the Trustee pursuant to subsection (b) or otherwise, the City shall as soon as possible determine if such event would be material under applicable federal securities law.

(d) If the City determines that knowledge of the occurrence of a Listed Event would be material under applicable federal securities law, the City shall promptly notify the Dissemination Agent and the Trustee in writing. Such notice shall instruct the Dissemination Agent to report the occurrence pursuant to subsection (f) and shall instruct the Trustee to report the occurrence to the Owners of the Bonds affected by the occurrence of such event.

(e) If in response to a request under subsection (b), the City determines that the Listed Event is not material, the City shall so notify the Dissemination Agent and the Trustee in writing and instruct the Dissemination and the Trustee to not report the event.

(f) If the Dissemination Agent has been instructed by the City to report the occurrence of a Listed Event, the Dissemination Agent shall promptly file a notice of such occurrence with the Municipal Securities Rulemaking Board and each Repository, with a copy to the Trustee. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(8) and (9) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to holders of affected Bonds pursuant to the Trust Agreement.

Section 6. Termination of Reporting Obligation. The City’s obligations under this Disclosure Agreement shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the City shall give notice of such termination on the same manner as for a Listed Event under Section 5(c) hereof.

Section 7. Dissemination Agent. The City may, from time to time, appoint or engage a Disseminating Agent to assist it in carrying out its obligations under this Disclosure Agreement, and may discharge any such Agent, with or without appointing a successor Dissemination Agent. The initial Dissemination Agent shall be BNY Western Trust Company. The Dissemination Agent may resign by giving thirty (30) days written notice to the City and the Trustee.

Section 8. Amendment; Waiver. Notwithstanding any other provision herein to the contrary, any provision in the Disclosure Agreement may be amended or waived (and the Trustee and the Dissemination Agent shall agree to any such amendment or waiver requested by the City, provided that neither the Trustee nor the Dissemination Agent shall be obligated to enter into any amendment or agree to any waiver that modifies or increases its duties or obligations hereunder), provided that the following conditions are satisfied:

(a) the amendment or waiver, if it relates to annual or event information to be provided, is made in connection with a change in circumstances that arises from a change in legal

requirements, change in law, or change in the identity, nature, or status of the City or type of business conducted;

(b) the undertakings herein, as proposed to be amended or waived, would have complied with the requirements of the Rule at the time of the primary offering of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances;

(c) the proposed amendment or waiver (i) is approved by Owners of the Bonds in the manner provided in the Trust Agreement for amendments to the Trust Agreement with the consent of Owners, or (ii) does not, in the opinion of the Trustee or nationally recognized bond counsel, materially impair the interest of Owners; and

(d) no amendment increasing or affecting the obligations or duties of the Dissemination Agent or the Trustee shall be made without the consent of either party.

If the annual financial information or operating data to be provided in the Annual Report is amended pursuant to the provisions hereof, the annual financial information containing the amended operating data or financial information shall explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

If an amendment is made to the undertaking specifying the accounting principles to be followed in preparing financial statements, the annual financial information for the year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. The comparison shall include a qualitative discussion of the differences in the accounting principles and the impact of the change in the accounting principles on the presentation of the financial information, in order to provide information to investors to enable them to evaluate the ability of the City to meet its obligations. To the extent reasonably feasible, the comparison shall be quantitative. A notice of the change in the accounting principles shall be sent to the Repositories.

Section 9. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the City from disseminating any other information, using the means of dissemination set forth in this Disclosure Agreement or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Agreement. If Agency chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Agreement, the City shall have no obligation under this Disclosure Agreement to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

Section 10. Default. In the event of a failure of the City to comply with any provision of this Disclosure Agreement, the Trustee at the written request of any Participating Underwriter or holders of at least a majority in aggregate amount of Outstanding Bonds, shall, but only to the extent indemnified to its satisfaction from and against any loss, cost, expense or liability of any kind whatsoever, including, without limitation, fees and expenses of its attorneys and additional fees and expenses of the Trustee, or any holder or beneficial owner of the Bonds may take such actions as may be necessary and appropriate, including seeking mandamus or specific performance by court order, to cause the City to comply with its obligations under this Disclosure Agreement. A default under this Disclosure Agreement shall not be deemed an Event of Default under the Trust Agreement, and the sole remedy under this Disclosure Agreement in the event of any failure of the City, the Trustee or the Dissemination Agent to comply with this Disclosure Agreement shall be an action to compel performance.

Section 11. Duties, Immunities and Liabilities of Dissemination Agent. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Agreement, and the City agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys' fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The Dissemination Agent shall be paid compensation by the City for its services provided hereunder in accordance with its schedule of fees as amended from time to time and all expenses, legal fees and advances made or incurred by the Dissemination Agent in the performance of its duties hereunder. The Dissemination Agent shall have no duty or obligation to review any information provided to them hereunder and shall not be deemed to be acting in any fiduciary capacity hereunder for the City, the Owners, or any other party. The obligations of the City under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

Section 12. Beneficiaries. The Disclosure Agreement shall inure solely to the benefit of the City, the Dissemination Agent, the Trustee, the Participating Underwriter and holders and beneficial owners from time to time of the Bonds, and shall create no rights in any other person or entity.

Section 13. Counterparts. This Disclosure Agreement may be executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

IN WITNESS WHEREOF, the parties hereto have caused their duly authorized officers to execute and deliver this Disclosure Agreement on the date first written above.

CITY OF MORGAN HILL

By: _____
City Manager

BNY WESTERN TRUST COMPANY,
as Trustee and Dissemination Agent

By: _____
Authorized Officer

EXHIBIT A

NOTICE TO MUNICIPAL SECURITIES RULEMAKING BOARD OF
FAILURE TO FILE ANNUAL REPORT

Name of Issuer: Morgan Hill Financing Authority

Name of Bond Issue: \$_____ Water Revenue Bonds, Series 2004

Date of Issuance: _____, 2004

NOTICE IS HEREBY GIVEN that the City of Morgan Hill (the "City") has not provided an Annual Report with respect to the above-named Bonds as required by Section 3 of the Continuing Disclosure Agreement, dated _____, 2004, executed by and between the City and BNY Western Trust Company, as Trustee and Dissemination Agent. The City anticipates that the Annual Report will be filed by _____.

Dated: _____, 20__.

BNY WESTERN TRUST COMPANY,
as Dissemination Agent on behalf of the City of
Morgan Hill

By: _____
Name: _____
Title: _____

cc: City of Morgan Hill, Director of Finance

APPENDIX F

DTC'S BOOK-ENTRY ONLY SYSTEM

[confirm that this is current] *The information in this Appendix concerning DTC and DTC's book-entry system has been obtained from sources that the Authority believes to be reliable, but neither the Authority nor the City takes any responsibility for the accuracy thereof. The Authority and the City give no assurances that (i) DTC, the Direct and Indirect Participants or others will distribute payments of principal, premium (if any) or interest with respect to the Bonds paid to DTC or its nominee as, the registered owner, to the Beneficial Owners, (ii) such entities will distribute redemption notices or other notices, to the Beneficial Owners, or (iii) an error or delay relating thereto will not occur.*

The Depository Trust Company ("DTC"), New York, New York, will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered certificate will be issued for the each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of each Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds. DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to DTC. If less than all of the Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, premium (if any) and interest payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Authority or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, the Authority or the Trustee, subject to any statutory or regulatory requirements as may be in effect from time to time. Principal, premium (if any) and interest payments with respect to the Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, Bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered in accordance with the provisions of the Trust Agreement.

APPENDIX G
SPECIMEN OF BOND INSURANCE POLICY

APPENDIX H
FORM OF NOTICE INVITING BIDS

CONSULTANT AGREEMENT
RICHARDS, WATSON & GERSHON, A PROFESSIONAL CORPORATION

THIS AGREEMENT is made this 6th day of October, 2004, by the CITY OF MORGAN HILL, a municipal corporation, ("CITY"), and Richards, Watson & Gershon, A Professional Corporation ("CONSULTANT").

RECITALS

The following recitals are a substantive part of this Agreement:

1. This Agreement is entered into pursuant to City Council approval on October 6, 2004.
2. CONSULTANT is qualified by virtue of experience, training, education, and expertise to accomplish these services.

AGREEMENT

THE PARTIES MUTUALLY AGREE AS FOLLOWS:

1. **Term of Agreement.** This Agreement shall cover services rendered from July 1, 2004, until June 30, 2005.
2. **Services to be Provided.** The services to be performed by CONSULTANT shall consist of special legal counsel services in the nature of bond counsel services and disclosure counsel services in connection with the issuance of water revenue bonds by or on behalf of the CITY.
3. **Compensation.** CONSULTANT shall be compensated as follows:
 - 3.1. **Amount.** Compensation under this Agreement shall not exceed \$33,500 for bond counsel services and \$20,000 for disclosure counsel services and shall be contingent upon closing of the bond financing.
 - 3.2. **Payment.** For work under this Agreement, payment shall be made per invoice.
 - 3.3. **Records of Expenses.** CONSULTANT shall keep accurate records of payroll, travel, and expenses. These records will be made available to CITY.
 - 3.4. **Termination.** CITY and CONSULTANT shall have the right to terminate this Agreement, without cause, by giving fifteen (15) days' written notice.

4. **Insurance Requirements.**

4.1. **Commencement of Work.** CONSULTANT shall not commence work under this Agreement until it has obtained CITY approved insurance. For general liability and automobile insurance policies, CONSULTANT shall provide CITY, prior to commencement of work, with a separate endorsement which states that the policy contains the following language:

- The CITY, its elected officials, officers, employees, agents and representatives are named as additional insureds; and,
- the insurer waives the right of subrogation against CITY and CITY'S elected officials, officers, employees, agents, and representatives; and,
- insurance shall be primary non-contributing.

CONSULTANT shall furnish CITY with copies of all policies or certificates subject to this Agreement, whether new or modified, promptly upon receipt. No policy subject to this Agreement shall be cancelled or materially changed except after thirty (30) days' notice by the insurer to CITY by certified mail.

4.2. **Workers Compensation Insurance.** CONSULTANT and all subcontractors shall maintain Worker's Compensation Insurance, if applicable.

4.3. **Insurance Types and Amounts.** CONSULTANT shall maintain general commercial liability and automobile insurance against claims and liabilities for personal injury, death, or property damage, providing protection of at least \$1,000,000 for bodily injury or death to any one person for any one accident or occurrence and at least \$1,000,000 for property damage. CONSULTANT shall also maintain professional liability insurance in an amount of \$1,000,000 per claim.

4.4. **Acceptability of Insurers.** All insurance required by this Agreement shall be carried only by responsible insurance companies licensed to do business in California. Insurance is to be placed with insurers with a current A.M. Best's rating of no less than A:VII.

4.5. **Provision of Agreement to Insurers.** CONSULTANT represents and warrants that they have provided a copy of this Agreement to their respective insurers, and the insurers are aware of all obligations pertaining to CONSULTANT as stated in this Agreement.

5. **Non-Liability of Officials and Employees of the CITY.** No official or employee of CITY shall be personally liable for any default or liability under this Agreement.

6. **Non-Discrimination.** CONSULTANT covenants there shall be no discrimination based upon race, color, creed, religion, gender, marital status, age, disability, national origin, or ancestry, in any activity pursuant to this Agreement.

7. **Independent Contractor**. It is agreed to that CONSULTANT shall act and be an independent contractor and not an agent or employee of CITY.
8. **Compliance with Law**. CONSULTANT shall comply with all applicable laws, ordinances, codes, and regulations of the federal, state, and local government.
9. **Ownership of Work Product**. All documents or other information developed or received by CONSULTANT for work performed under this agreement shall be the property of CITY. CONSULTANT shall provide CITY with copies of these items upon demand or upon termination of this Agreement.
10. **Conflict of Interest and Reporting**. CONSULTANT shall at all times avoid conflict of interest or appearance of conflict of interest in performance of this Agreement.
11. **Notices**. All notices shall be personally delivered or mailed, via first class mail to the below listed address. These addresses shall be used for delivery of service of process. Notices shall be effective five (5) days after date of mailing, or upon date of personal delivery.

Address of CONSULTANT is as follows:

Richards, Watson & Gershon
355 South Grand Avenue, Suite 4000
Los Angeles, California 90071

Address of CITY is as follows:

Finance Director	with a copy to:
City of Morgan Hill	City Clerk
17555 Peak Avenue	17555 Peak Avenue
Morgan Hill, CA 95037	Morgan Hill, CA 95037

12. **CONSULTANT'S Proposal**. This Agreement shall include CONSULTANT'S proposal or bid, which is incorporated herein. In the event of any inconsistency between the terms of the proposal and this Agreement, this Agreement shall govern.
13. **Licenses, Permits, and Fees**. CONSULTANT shall obtain a City of Morgan Hill Business License, all permits, and licenses as may be required by this Agreement.
14. **Familiarity with Work**. By executing this Agreement, CONSULTANT warrants that: (1) it has investigated the work to be performed; (2) it has investigated the site of the work and is aware of all conditions there; and (3) it understands the difficulties and restrictions of the work under this Agreement. Should CONSULTANT discover any conditions materially differing from those inherent in the work or as represented by CITY, it shall immediately inform CITY and shall not proceed, except at CONSULTANT'S risk, until written instructions are received from CITY.
15. **Time of Essence**. Time is of the essence in the performance of this Agreement.

16. **Limitations Upon Subcontracting and Assignment.** Neither this Agreement or any portion shall be assigned by CONSULTANT, without prior written consent of CITY.

17. **Authority to Execute.** The persons executing this Agreement on behalf of the parties warrant that they are duly authorized to execute this Agreement.

18. **Indemnification.**

18.1. For claims arising from CONSULTANT'S professional acts or omissions, CONSULTANT agrees to protect, defend and hold harmless CITY and its elective or appointive boards, officers, agents, and employees from any and all claims, liabilities, expenses, or damages of any nature, including reasonable attorneys' fees, for injury or death of any person, or damage to property, or interference with use of property, to the extent arising out of the negligence performance and/or willful acts or omission of CONSULTANT, CONSULTANT'S agents, officers, employees, subcontractors, or independent contractors hired by CONSULTANT.

18.2. For any other claim arising from any other act or omission, performance or non-performance by CONSULTANT under this Agreement, CONSULTANT agrees to protect, defend and hold harmless CITY and its elective or appointive boards, officers, agents, and employees from any and all claims, liabilities, expenses, or damages of any nature, including reasonable attorneys' fees, for injury or death of any person, or damage to property, or interference with use of property, to the extent arising out of this Agreement by CONSULTANT, CONSULTANT'S agents, officers, employees, subcontractors, or independent contractors hired by CONSULTANT.

18.3. The only exception to CONSULTANT'S above-named responsibilities to protect, defend, and hold harmless CITY is due to the sole negligence of CITY as adjudged by a court of competent jurisdiction. CONSULTANT shall bear any initial burden of protection, defense, and hold harmless until such court judgment is rendered.

18.4. This agreement shall apply to all liability, regardless of whether any insurance policies are applicable. Policy limits do not act as a limitation upon the amount of indemnification to be provided by CONSULTANT.

19. **Modification.** This Agreement constitutes the entire agreement between the parties and supersedes any previous agreements, oral or written. This Agreement may be modified or provisions waived only by subsequent mutual written agreement executed by CITY and CONSULTANT.

20. **California Law.** This Agreement shall be construed in accordance with the laws of the State of California. Any action commenced about this Agreement shall be filed in the Santa Clara County Superior Court.

21. **Interpretation.** This Agreement shall be interpreted as though prepared by both parties.

22. **Preservation of Agreement.** Should any provision of this Agreement be found invalid or unenforceable, the decision shall affect only the provision interpreted, and all remaining provisions shall remain enforceable.

IN WITNESS THEREOF, these parties have executed this Agreement on the day and year shown below.

ATTEST:

THE CITY OF MORGAN HILL

City Clerk

City Manager

Date: _____

Date: _____

APPROVED:

“CONSULTANT”

Risk Manager

By: William L. Strausz

Date: _____

Date:

APPROVED AS TO FORM:

City Attorney

Date: _____

FINANCIAL ADVISOR AGREEMENT RBC DAIN RAUSCHER INC.

THIS AGREEMENT is made this 6th day of October, 2004, by the CITY OF MORGAN HILL, a municipal corporation, ("CITY"), and RBC DAIN RAUSCHER INC., California corporation ("CONSULTANT").

RECITALS

The following recitals are a substantive part of this Agreement:

1. This Agreement is entered into pursuant to City Council approval on October 6, 2004.
2. CONSULTANT is qualified by virtue of experience, training, education, and expertise to accomplish these services.

AGREEMENT

THE PARTIES MUTUALLY AGREE AS FOLLOWS:

Term of Agreement. This Agreement relates to the issuance by the City of the Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 ("OBLIGATION") which the City intends to issue in order to raise proceeds to fund certain capital improvements of its Water Utility and covers services rendered from the date of this Agreement until the closing of the OBLIGATION.

Services to be Provided. The services to be performed by CONSULTANT shall consist of those services as provided in Appendix A herein.

Compensation. CONSULTANT shall receive a fee of \$75,000.00 for services rendered under this Agreement plus reimbursement of any out-of-pocket expenses incurred by CONSULTANT which are directly related to the issuance of the OBLIGATION. Payment of CONSULTANT'S fee and expenses is contingent upon the closing of the OBLIGATION and will be paid from proceeds of the OBLIGATION at the time of closing.

Termination. CITY and CONSULTANT shall have the right to terminate this Agreement, without cause, by giving thirty (30) days' written notice.

Insurance Requirements.

Commencement of Work. CONSULTANT shall not commence work under this Agreement until it has obtained CITY approved insurance. For a general liability policy, CONSULTANT shall provide CITY, prior to commencement of work, with a separate endorsement that states that the policy contains the following language:

- (a) The CITY, its elected officials, officers, employees, agents and representatives are named as additional insureds; and,
- (b) the insurer waives the right of subrogation against CITY and CITY'S elected officials, officers, employees, agents, and representatives; and,
- (c) insurance shall be primary non-contributing.

CONSULTANT shall furnish CITY with copies of certificates subject to this Agreement, whether new or modified, promptly upon receipt. The insurer will endeavor to give CITY thirty (30) days' notice if a policy subject to this Agreement shall be cancelled or materially changed.

Workers Compensation Insurance. CONSULTANT and all subcontractors shall maintain Worker's Compensation Insurance, if applicable.

Insurance Types and Amounts. CONSULTANT shall maintain general commercial liability insurance against claims and liabilities for personal injury, death, or property damage, providing protection of at least \$1,000,000 for bodily injury or death to any one person for any one accident or occurrence and at least \$1,000,000 for property damage. CONSULTANT shall also maintain professional liability insurance in an amount of \$1,000,000 per claim.

Acceptability of Insurers. All insurance required by this Agreement shall be carried only by responsible insurance companies licensed to do business in California. Insurance is to be placed with insurers with a current A.M. Best's rating of no less than A:VII.

Non-Liability of Officials and Employees of the CITY. No official or employee of CITY shall be personally liable for any default or liability under this Agreement.

Non-Discrimination. CONSULTANT covenants there shall be no discrimination based upon race, color, creed, religion, gender, marital status, age, disability, national origin, or ancestry, in any activity pursuant to this Agreement.

Independent Contractor. It is agreed to that CONSULTANT shall act and be an independent contractor and not an agent or employee of CITY.

Compliance with Law. CONSULTANT shall comply with all applicable laws, ordinances, codes, and regulations of the federal, state, and local government.

Ownership of Work Product. All documents or other information developed or received by CONSULTANT for work performed under this agreement shall be

the property of CITY. CONSULTANT shall provide CITY with copies of these items upon demand or upon termination of this Agreement.

Conflict of Interest and Reporting. CONSULTANT shall at all times avoid conflict of interest or appearance of conflict of interest in performance of this Agreement.

Notices. All notices shall be personally delivered or mailed, via first class mail to the below listed address. These addresses shall be used for delivery of service of process. Notices shall be effective five (5) days after date of mailing, or upon date of personal delivery.

Address of CONSULTANT is as follows:

Richard Morales, Principal
RBC Dain Rauscher Inc.
345 California Street, Ste. 2800
San Francisco, CA 94104
Attn.: Fixed Income Banking

Address of CITY is as follows:

Finance Director	with a copy to:
City of Morgan Hill	City Clerk
17555 Peak Avenue	17555 Peak Avenue
Morgan Hill, CA 95037	Morgan Hill, CA
	95037

CONSULTANT'S Proposal. This Agreement shall include CONSULTANT'S proposal or bid, which is incorporated herein. In the event of any inconsistency between the terms of the proposal and this Agreement, this Agreement shall govern.

Familiarity with Work. By executing this Agreement, CONSULTANT warrants that (1) it has investigated the work to be performed; (2) it has investigated the site of the work and is aware of all conditions there; and (3) it understands the difficulties and restrictions of the work under this Agreement. Should CONSULTANT discover any conditions materially differing from those inherent in the work or as represented by CITY, it shall immediately inform CITY and shall not proceed, except at CONSULTANT'S risk, until written instructions are received from CITY.

Time of Essence. Time is of the essence in the performance of this Agreement.

Limitations Upon Subcontracting and Assignment. Neither this Agreement or any portion shall be assigned by CONSULTANT, without prior written consent of CITY.

Authority to Execute. The persons executing this Agreement on behalf of the parties warrant that they are duly authorized to execute this Agreement.

Disclosure.

CITY acknowledges that it is responsible for the contents of its disclosure document and is subject to and may be held liable under federal securities laws for violations thereof, including misleading or incomplete disclosure. To the extent permissible by law, CITY agrees to indemnify and hold CONSULTANT harmless against any losses, claims, damages or liabilities to which it may become subject under federal or state securities laws or regulations, at common law or otherwise (including in settlement of any litigation if such settlement is effected with the written consent of the CITY), insofar as such losses, claims, damages or liabilities (or actions in respect thereof) arise out of or are based upon omission to state in the disclosure document a material fact required to be stated therein or necessary to make the statements therein not misleading; and will reimburse CONSULTANT for any legal or other expenses reasonably incurred by it in connection with investigating or defending any such loss, claim, damage, liability or action.

Indemnification.

All actions taken and all recommendations made by CONSULTANT in performing its duties under this Agreement will be based on its best professional judgment with the goal of obtaining the most favorable terms for the CITY and is not a guarantee of result. However, for claims arising from CONSULTANT'S professional acts or omissions, CONSULTANT agrees to protect, defend and hold harmless the CITY and its elective or appointive boards, officers, agents, and employees from any and all claims, liabilities, expenses, or damages of any nature, including reasonable attorneys' fees, for injury or death of any person, or damage to property, or interference with use of property, to the extent arising out of the grossly negligent performance and/or willful acts or omission of CONSULTANT, CONSULTANT'S agents, officers, employees, subcontractors, or independent contractors hired by CONSULTANT; provided that such losses, claims, damages or liabilities are not attributable to the CITY'S own negligence or misconduct in carrying out its duties.

For any other claim arising from any other act or omission, performance or non-performance by CONSULTANT under this Agreement, CONSULTANT agrees to protect, defend and hold harmless CITY and its elective or appointive boards, officers, agents, and employees from any and all claims, liabilities, expenses, or damages of any nature, including reasonable attorneys' fees, for injury or death of any person, or damage to property, or interference with use of property, to the extent arising out of this Agreement by CONSULTANT, CONSULTANT'S agents, officers, employees, subcontractors, or independent contractors hired by CONSULTANT.

The only exception to CONSULTANT'S above-named responsibilities to protect, defend, and hold harmless CITY is due to the sole negligence of CITY as adjudged by a court of competent jurisdiction. CONSULTANT shall bear any initial burden of protection, defense, and hold harmless until such court judgment is rendered.

This Agreement shall apply to all liability, regardless of whether any insurance policies are applicable. Policy limits do not act as a limitation upon the amount of indemnification to be provided by CONSULTANT.

Modification. This Agreement constitutes the entire agreement between the parties and supersedes any previous agreements, oral or written. This Agreement may be modified or provisions waived only by subsequent mutual written agreement executed by CITY and CONSULTANT.

California Law. This Agreement shall be construed in accordance with the laws of the State of California. Any action commenced about this Agreement shall be filed in the Santa Clara County Superior Court.

Interpretation. This Agreement shall be interpreted as though prepared by both parties.

Preservation of Agreement. Should any provision of this Agreement be found invalid or unenforceable, the decision shall affect only the provision interpreted, and all remaining provisions shall remain enforceable.

IN WITNESS THEREOF, these parties have executed this Agreement on the day and year shown below.

ATTEST:

THE CITY OF MORGAN HILL

City Clerk

Date: _____

City Manager

Date: _____

APPROVED:

"CONSULTANT"

Risk Manager

Date: _____

By:

Date: _____

APPROVED AS TO FORM:

City Attorney

Date: _____

APPENDIX A

FINANCIAL ADVISOR SCOPE OF SERVICES

RBC Dain Rauscher Inc. ("RBC Dain") proposes to act as financial advisor to the City of Morgan Hill, California ("City") on the issuance, through a competitive sale process, of the Morgan Hill Financing Authority Water Revenue Bonds, Series 2004 ("Bonds") the proceeds of which will be used to fund certain capital improvements to the Water Utility of the City. To fulfill these duties as financial advisor, we agree to perform the following:

1. Scope of Services

- (a) Analyze the financing alternatives available to the City, taking into account its borrowing capacity, future financing needs, policy considerations, and such other factors as we deem appropriate to consider.
- (b) Recommend a plan for the issuance of the Bonds that will include: (1) the type of bonds (current interest, capital appreciation, deferred income, etc.); (2) the date of issue; (3) principal amount; (4) interest structure (fixed or variable); (5) interest payment dates; (6) a schedule of maturities; (7) early redemption options; (8) security provisions; and (9) other matters that we consider appropriate to best serve the City's interests.
- (c) Advise the City of current conditions in the relevant debt market, upcoming bond issues, and other general information and economic data which might reasonably be expected to influence interest rates, bidding conditions or timing of issuance.
- (d) Organize and coordinate the financing team. Unless otherwise directed by the City, we will assist in the selection of trustee; electronic competitive bidding provider; printer and any other service providers as needed for the transaction. Such service providers will be compensated by the City from proceeds of the Bonds.
- (e) Work with bond counsel on the transaction, whom you will retain and compensate from proceeds of the Bonds. Such bond counsel firm will be a recognized municipal bond firm, will prepare the proceedings, provide legal advice concerning the steps necessary to be taken to issue the Bonds, and issue an unqualified opinion (in a form standard for the particular type of financing) approving the legality of the Bonds and (as applicable) tax exemption of the interest paid thereon. In addition, bond counsel will issue an opinion to the effect that the

disclosure document does not contain an untrue statement of a material fact or omit to state a material fact necessary in order to make the statements contained therein, in light of the circumstances under which they were made, not misleading. Generally, working with bond counsel will mean coordinating with the attorneys and assisting in the financial advisory aspects of preparing appropriate legal proceedings and documents, including documents concerning any required election.

(e) Assist in the City's preparation of the Preliminary Official Statement ("POS") and the Official Statement ("OS") or equivalent document as the particular transaction may require. City will retain a disclosure counsel law firm to take primary responsibility for the preparation of the POS and OS. Such disclosure counsel will be compensated from proceeds of the Bonds.

(f) In connection with a competitive sale, RBC Dain will:

- i. coordinate the preparation of the Official Notice of Sale and Bid Form (containing provisions recognized by the municipal securities industry as being consistent with the securities offered for sale) and other such documents which you may request or deem appropriate;
- ii. submit all such documents for examination, approval, and certification by appropriate officials, employees, and agents of the City, including bond counsel;
- iii. coordinate delivery of these documents to a list of prospective bidders;
- iv. where appropriate, organize investor meetings;
- v. coordinate the receipt of bids;
- vi. advise as to the best bid, including acceptance or rejection of the best bid;
- vii. if a bid is accepted, coordinate the delivery of and payment for the Bonds;
- viii. assist in verification of final closing figures;
- ix. provide copies of documents to the purchaser of the Bonds in accordance with the terms of the Official Notice of Sale and Bid Form.

(g) Make recommendations as to credit rating(s) for the proposed Bonds and, should the City seek a rating, coordinate the process of working

with the rating agency or agencies and assist in the preparation of presentations as necessary.

- (h) Make recommendations as to obtaining municipal bond insurance, a liquidity facility or other credit enhancement for the Bonds and, should the City seek any such credit enhancement, coordinate the process and assist in the preparation of presentations as necessary.
- (i) Attend meetings of governing bodies of the City, its staff, representatives or committees as requested.
- (j) After closing, RBC Dain will deliver to the City, bond counsel and the trustee definitive debt records, including a schedule of annual debt service requirements on the Bonds. The City acknowledges that advice and recommendations involve professional judgement on our part and that the results cannot be, and are not, guaranteed.